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EDITORS

Western Europe

Professor Barry J. Davies

Professor of Marketing, University of Gloucestershire, UK
bdavies@glos.ac.uk

The Rest of the World

Professor Claudio Vignali

Arnold Ziff Chair in Retailing, Leeds Metropolitan University, UK
c.vignali@leedsmet.ac.uk

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leo.dana@cantebury.ac.nz

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kaufmann.r@unic.ac.cy

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srenko@efzg.hr

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sommer@hs-alsib.de

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jantima@su.ac.th

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vitor.ambrosio@esthe.pt

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nirmaalya@bmaindia.com

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ihnhee@kumoh.ac.kr

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kanzlei.schackmar@arcor.de

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r.raj@leedsmet.ac.uk

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Graduate School of Economics, University of Zagreb
dtipuric@efzg.hr

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Shanxi University of Finance and Economics
xuyanqjh@163.com

ASSOCIATE EDITORS

Gianpaolo Vignali

Manchester Metropolitan University, UK
g.vignali@mmu.ac.uk

Dr. Mirko Palic

Graduate School of Economics, University of Zagreb
mpalic@efzg.hr

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INSTITUTE FOR ONE WORLD HEALTH (IOWH): SHAPING THE FUTURE WHEN LIFE IS HARD ENOUGH

TERESA MARTINELLI-LEE
UNIVERSITY OF LA VERNE

DIANE MONJAY
UNIVERSITY OF LA VERNE

ISSAM A. GHAZZAWI
UNIVERSITY OF LA VERNE

JEANNY LIU
UNIVERSITY OF LA VERNE

ABSTRACT

This case chronicles an impoverished family in Bihar that has experienced the destructive effects of Visceral Leishmaniasis (VL) with neighbours and family. The family lives in fear for the health and wellbeing of their children. The case outlines the unique needs of a population affected by a neglected disease for which there is no market for a cure in the developed world, and therefore a lack of incentive to develop an effective and cost-efficient treatment. Owing to her professional background in both public and private enterprises, along with her personal desire to make a difference, this case study also chronicles the inspirational brainchild of Victoria Hale, PhD, her husband, Ahvie Herskowitz, MD, the Institute of OneWorld Health (iOWH), and a relationship building of non-typical public-private partnership. This case highlights the need for a unique partnership, outlines the struggles in launching one, and the ensuing challenges faced in maintaining funding for a development project that will not see fruition for several years.

KEYWORDS - Public private partnerships (PPP) Institute for OneWorld Health, Visceral leishmaniasis treatment Pharmaceutical organisations, Non-profit, Bihar, India

INSTITUTE FOR ONEWORLD HEALTH (IOWH): SHAPING THE FUTURE WHEN LIFE IS HARD ENOUGH

Sabal Mishra lived with his five brothers and sisters, his mother, father, and his 65-year-old grandmother on a small farm in the Bihar region of India, one of the poorest states in the country. He was seven years old. He was the second to the youngest, with a younger sister, four years old, an older sister, 12, and two brothers ages eight and ten. Sabal lived in a one room, mud-plastered hut. The family used dung from their cattle to augment the mud that filled the cracks between the reeds and thatch that comprised his family's home. At seven years, he was responsible for his family's few cattle, which he watched over carefully during the day. Sometimes he fell asleep under the acacia tree not far from the termite mounds. When he was younger, he used to jab sticks into the mound and watch the tiny insects cling to the sticks. But at of seven, he no longer had time to marvel at such things. An occasional nap in the shade of the acacia tree was the sole reprieve from his daily chores and responsibilities. As Sabal napped, swatting at the troublesome sandflies, little did he know how his life would soon collide with the work of a determined pharmaceutical scientist, and how her passion to fight one of India's most neglected diseases would ultimately save his life.

Indeed, while Sabal napped, half a world away, Dr. Victoria Hale of the Institute for OneWorld Health was preparing plans to not only save Sabal's life, but also save those of thousands of improvised families throughout India.

A FAMILY WORRIES

Not unlike other Indians in Bihar, Sabal's family was at increased risk of disease and illness due to existing poor housing and sanitation conditions in the severely impoverished state. In the spring of 2006, Sabal's family lived many miles from the nearest health clinic, a fact that worried his mother. The only road was poorly maintained, pot-holed, often flooded in the rainy season, and certainly treacherous to travel. Weather permitting, the family occasionally went into town primarily with the older children, while Dadi (grandmother) stayed home with the youngest, Shreela. They made clothing and sold the items in town to supplement their meagre income, which was about fifty-six U.S. dollars per year. Barely keeping the family fed, this amount did not leave much for luxuries such as medicines. Naturally, Mother often worried. What would they do should one of the children get sick? Could they get them to the clinic in time? But worse could they even afford treatment?

Sabal's mother, Pakhi, had reason to worry. Many of her neighbours had suffered and died of the dreaded kala-azar what locals called the black fever also known as visceral leishmaniasis (VL). While the disease is endemic (See Exhibit 1 Countries where Leishmaniasis is Endemic) in sixty-five countries worldwide, 90 per cent of kala-azar (Hindi for black fever) cases occur in India, Bangladesh, Nepal, Sudan, and Brazil (Hale, Woo, & Lipton 2005). It is estimated that approximately 200,000 people die annually because of the widespread disease (Hale, Woo, & Lipton 2005). Leishmaniasis often strikes the poor and the malnourished that typically are unable to afford expensive treatments.

Pakhi, Sabal's mother, remembered her younger brother, Rajak, who died in 1991 of kala-azar when he was just fifteen years old. His symptoms started at thirteen. At the time, Pakhi's parents hastily took him to the local clinic. He was treated with some kind of medicine, which the clinic doctor called an antimonial-antibiotic. Enduring extremely painful injections, Rajak seemed to have grown even more ill. His arms and legs became thinner and thinner, as his swollen belly grew ever more distended.

The medicine was incredibly expensive prompting Pakhi's family to sell their animals, and most of their assets in order to afford the treatments. As a teenager, Rajak was a major contributor to the family's income. Subsequently, his illness not only had a devastating impact emotionally on the family, but economically as well.

Many prayers were said, but Rajak did not get better. Over several weeks and much expense, the family persisted in travelling to the clinic so Rajak could get his injections. Unable to eat, organs bulging under his rib cage, and unbelievably emaciated, Rajak slowly and painfully died. The clinic doctors said that the medicine they used was no longer as effective as it used to be. The parasite that caused kala-azar had grown resistant to it. The image of her dying brother stayed with Pakhi.

Over the years, Pakhi knew many children and adults that had succumbed to the black fever. The families sold all their animals and assets to pay for their children's treatment, and often went into debt that carried over to subsequent generations. Sometimes the medicine worked and the child lived. However, when the next child or a parent became symptomatic with kala-azar, there was nothing left and certainly no way to afford the expensive treatments. As the next family member died, the entire family would literally disintegrate.

Yet, Pakhi heard medicines existed that could provide a cure. But they require many weeks of treatment and expensive hospitalisation. Further, the medicines are toxic and can ravage an already compromised body. One such treatment is amphotericin B, considered a virtual cure (Olliaro, Darley, Laxminarayan, & Sundar 2009). Typically used in the U.S. for fungal infections, it is a treatment of last resort. Indeed, in U.S. hospitals clinicians have nicknamed it 'amphoterrible' (Gorman 1993). Unfortunately, the total cost of kala-azar for a family in India may be as much as US\$210 – at least two and a half times more than the average per capita income ((Vanlerberghe, et al. 2007). This was nearly four times Sabal's family income.

So Pakhi said her prayers, and held fast to her children. She prayed that kala-azar would leave her family alone. Life was hard enough.

VISCERAL LEISHMANIASIS

Visceral leishmaniasis (VL), locally called 'black fever' generally referred to as kala-azar is a tropical parasite based disease. Often fatal, it occurs primarily on the Asia continent and predominately in northern India (Bhattacharya, Sur, & Karbwang 2006). Affecting primarily children under the age of six, the parasite (*leishmania donovani*) presents its victims with intermittent fever, anaemia, enlarged spleen and liver and the gauntness of emaciation (Bora 1999). The clinical severity of VL is further manifested by the need to diagnose paediatric patients, which requires bone marrow extraction for intracellular demonstration, which undoubtedly is invasive and procedurally a particularly painful experience for the children (Desjeux 1992).

Kala-azar is an insidious disease that strikes all ages, but especially the young and vulnerable (see Exhibit 2 Kala-azar Cases and Deaths in India since 2002). The fevers are incessant and chronic. The disease wipes out bone marrow, including red blood cells, white blood cells and platelets. The destruction of the immune system further increases a person's vulnerability to infection (Narain et al. 2010). Suffering anaemia, its victims also lose the ability to clot blood. Internal bleeding is common, which causes black discolouration of the skin; hence, its name 'black fever' translated kala-azar (Hindi). The body becomes emaciated. The belly slowly distends and bloats due to toxins that enlarge the liver and spleen, making a mockery of the emaciated arms and legs. Left untreated, the kala-azar kills up to 95 per cent of its victims. In the last decade, kala-azar has been associated with HIV/AIDS, and the risk for co-infection has risen (Narain et al. 2010).

Visceral leishmaniasis is considered a fatal systemic infection caused by the *Leishmania* parasites (see Exhibit 3 Life Cycle of Leishmaniasis) (Kolaczinski et al. 2008). The parasite is transmitted through the bite of a simple sandfly. Often, farmers who apply insecticides to their cattle to relieve their animals of biting insects and subsequent disease, unwittingly create an environment where the sandfly spends considerably more time with human hosts (Kolaczinski et al. 2008). In fact, the environment around the acacia tree and termite mounds is especially prone to sandfly infestations (Sundar, Jha, Thakus, Sinha, Bhyattacharya 2007). The mode of transmission in India is simple transmission to humans through the bite of the sandfly, unlike other parts of the world, i.e., Africa,

where dogs are also hosts to the *Leishmania* parasite. This makes eradication of VL easier in Bihar, since the disease is contained to the human population (Sundar, Jha, Thakus, Sinha, Bhyattacharya 2007). Other key factors that contribute to the dilemma in Bihar include dismally poor housing and efficient sanitation conditions. These conditions subsequently figure in the spread of the sand fly vector since it breeds in the cracks of mud-plastered houses and moist soils (Boelaert et al 2009).

THE STATE OF BIHAR, INDIA: AN OVERVIEW

Bihar's poverty and inadequate healthcare system can be traced to its history with economic and political strife. With an extensive history of religious preachers, princes, emperors and great warriors, the people of Bihar have endured a variety of rulers and governments since the 6th century B.C. Following British rule from 1765 to 1947, Bihar received statehood independence under India's unification of states. Filled with mythological and historical beauty, Bihar has a culture steeped in higher learning, art, literature, religion and the spiritualism of Buddha and Mahavira. Because of its cultivation in mystical enlightenment, Bihar is known as the ancient land of Buddha.

Bihar is indeed one of the poorest states in India, compared to the national average of 29 per cent nearly 40 per cent of Bihar's population lives below the poverty line (Boelaert et al 2009). Even though Bihar has fertile agricultural lands and substantial mineral resources, the region remains one of India's minimally developed states (Boelaert et al 2009). In the 1990s inasmuch as the whole of India was experiencing economic growth, Bihar was the country's only state to experience decline of per capita income (Boelaert et al 2009). Historical significance is given to the region as having the world's first seat of higher learning, the establishment of an administration system of governance and the development of the science of economics. These institutions continued to flourish until the mid 7th century A.D. when during the Gupta ruling period northern India and particularly Bihar became victim to Muslim invaders. Thus, began the continual influx of change and loss of political, economic, and cultural stability of Bihar and India as a whole.

Bihar is also well known as the remote corner of India where British rule was brought into question by national freedom leader Gandhiji, better known as Gandhi. In 1917, Gandhiji's distinguished actions resulted in India earning its independence from British sovereignty. With merely a mid 19th century establishment of governance, the State of Bihar retains a young status as an area of commerce and economy, politics and governance, and culture and religion. Currently, Bihar is incorporated through thirty-eight separate decentralised administrative districts each headed by a Deputy Commissioner with executive governance responsibilities (Government of Bihar 2010). Such command includes maintaining a magisterial authority as in law and order, but not police administration, which is delegated to the Superintendent of Police. While the Deputy Commissioner, as the collector, is responsible for revenue collection, disbursement, and recovery.

While Bihar is primarily an agrarian based economy, because of its fertile and productive soil it has a well-established textile industry connected to both trading and transportation activities (see Exhibit 4 the State of Bihar at a Glance). The primary producers of fruits and vegetables, several districts of Bihar have production mills manufacturing rice, sugar, and edible oils. Although the region of Bihar has been inundated by economic and political strife, the people of Bihar have preserved their rich cultural, spiritual, and religious traditions. The seats of learning, art, dance, and music have experienced a renaissance that has reversed the den of uncertainty bringing back the people's rich and cultural heritage.

The growth of economic and social development however has been hindered by the vulnerability in both health and welfare in many of the 38 districts. Several primary diseases have affected the people of this region especially the poorest of the poor who encounter malaria, viral fevers, Hepatitis B, nutrition, and cancer (breast, lung, prostate, and colon) health issues. Of these, the Ministry of Health has identified visceral leishmaniasis (VL) as a key disease because of its prevalence in the Indian subcontinent. In 2005, the Ministry of Health launched a VL elimination initiative built on early diagnosis followed by rapid test and treatment. The primary healthcare services in both hospitals and clinics used the oral drug paromomycin as its main strategy of attack. In rural areas, VL patients were registered, traced to their homes and interviewed to obtain valuable records. Other than treatment

regimens and costs incurred, both patient and doctor delays were recorded to evaluate treatment outcomes corollaries. To meet the target set by the Ministry of Health' for VL elimination, active case strategies and partnerships are crucial especially when coping with rural healthcare networks, which are capricious at best.

What seems to contribute to this level of socio-economic deficiency is the high level of illiteracy, a corrupt political system, and inadequate if not defunct healthcare system. However, such harsh economic conditions were not always the case. The last two centuries found Bihar having both cultural and economical stability based on three crops: sugar, cotton, and opium. As the population grew attributable to such agricultural health, Bihar's socio-political leaders did not foresee conditions by which agricultural prosperity would potentially dwindle. Population growth did not account for balance between natural resources, soil fertility, and recovery. As a result, the economic fortitude of the region began to dwindle. The new millennium ushered a condition for increased poverty and prevalence of tropical diseases.

For most of the districts of the State of Bihar, visceral leishmaniasis is endemic. Poverty is the lead determinant of this insidious disease that is seemingly predisposed to affect poor populations who have little to no access to healthcare facilities nor can afford long-term treatment. As such, with nearly 200 million people at risk of contracting the disease, the governments of Bangladesh, Nepal, and India launched a joint public health programme to eliminate VL by the year 2012 with the collaborative partnerships with nongovernmental organisations (NGOs) and intergovernmental organisations (IGOs) and other cross-national stakeholders (Kaenzig 2009). Further partnering with non-profit pharmaceutical companies, regional and state government have embarked on local drug production, in addition to R&D to unravel the causative parasitic agent as a means to reduce risk and improve patient treatment.

INSPIRATIONAL ENLIGHTENMENT

Dr. Victoria Hale, a pharmaceutical scientist, had garnered broad experience in both the government (Food and Drug Administration), as well as Industry. Based in South San Francisco, she had worked for Genentech, a biotechnology company (iOWH 2010a). Later, she became the founder,

with her physician husband, Ahvie Herskowitz, as co-founder, of the Institute for OneWorld Health (iOWH), a non-profit pharmaceutical company (iOWH 2010a).

In late 1999, Victoria Hale attended the Institute of Tropical Medicine conference in Antwerp, Belgium, where Dr. Shyam Sundar, an Indian cardiologist, and expert on visceral leishmaniasis, was pounding his fist during his talk about the world's failure to fight this disease (see Exhibit 5 Dr. Sundar in Bihar). He railed that there was an effective and safe treatment for kala-azar, and an inexpensive one that scientists had known about since the 1960s. It was paromomycin, an amino-glycoside antibiotic. All the amino-glycosides were screened in the 1960s for activity against the leishmania parasite, and only paromomycin was active. Paromomycin was off patent, thus as a generic it would be relatively inexpensive to manufacture.

Victoria was moved and inspired by Dr. Sundar and approached him after the conference. Dr. Sundar invited both Victoria Hale and her husband Ahvie Herskowitz, also a cardiologist and a Clinical Professor of Medicine at the University of California in San Francisco, to visit his free clinic in Muzaffarpur, Bihar to see the devastation first hand of visceral leishmaniasis (see Exhibit 5 and Exhibit 8).

Victoria Hale visited Dr. Sundar's clinic in spring 2000. Dr. Herskowitz, who accompanied her during later visits observed, 'Bihar transports you back in time. Yet, the people live their lives, move forward, and are brilliantly spiritual' (Interview Dr. Ahvie Herskowitz, October 15, 2010). In fact, according to Dr. Herskowitz, Bihar has significant historical importance. One of the world's earliest universities was established in Bihar in 900 A.D. and Bihar is where Buddha became enlightened company (Government of Bihar 2010). Due to this historical and spiritual significance, throughout the year there is one functional road in Bihar, yet it is maintained through a partnership with a Japan company (Interview Dr. Ahvie Herskowitz, October 15, 2010). Tourists and those seeking spiritual enlightenment are able to travel to the region because of this well maintained road.

According to Dr. Herskowitz, despite this attempt to provide navigable roadways there are still challenges. Dr. Herskowitz explains, 'This is a state where most families survive on less than a

dollar a day, and many exist on less than fifty cents per day' company (Interview Dr. Ahvie Herskowitz, October 15, 2010). In fact, although the caste system in India is certainly now illegal, it is still a practiced reality outside major cities. Nevertheless, the lowest of the low, often called the 'rat eaters,' encompass many of the people of Bihar.

Reminiscing, Dr. Sundar explained that his own mother suffered from the kala-azar, but she ultimately survived. He was passionate about the people, and as passionate to find a better way to treat and eradicate this devastating disease. During visits to Bihar, Drs. Hale and Herskowitz asked people they met what disease they were most afraid of, especially for their children. Was it malaria? Was it diarrhea? No, they answered, it was the dreaded kala-azar.

Dr. Sundar Rails against VL

During early discussions with Drs. Hale and Herskowitz, Dr. Sundar explained how he had worked with the World Health Organisation (WHO) in the mid-1980s, spearheading a series of encouraging Phase II studies with paromomycin, in the hope of bringing the drug closer to the leishmania market. The tragedy, indeed the crime, he said was that no one was doing anything more with it, while thousands died horrible deaths, unable to afford existing approved medicines or suffering from toxic side effects (Dusky 2007). However, there was not a profitable market for paromomycin in the developed world. The poorest countries where VL was endemic could not afford the expensive and lengthy Phase III studies necessary to bring the product to market. So it languished on the shelf at the World Health Organisation.

The World Health Organisation's (WHO) recommended treatment regimen for VL was a 30-day course of antimonials, (i.e. Pentostam, an antiprotozoan drug) at US\$28 per course for the generic (Vanlerberghe et al. 2007). Although considered a good value, antimonials are not ideal drug choices. They have to be administered intravenously over 28-30 days, require hospitalisation and are painful at the site of infusion. In addition, they can have rare but serious side effects such as cardio, pancreas and liver toxicity (Vanlerberghe et al. 2007). In fact, resistance to antimonials has been reported in up to 65 per cent of patients in some villages of Bihar, India (Vanlerberghe et al. 2007). Amphotericin

B was effective, and if the patient survived the treatment, it was close to a 100 per cent cure. However, toxicities and costs were clearly less than optimal. A new option to treat VL would be needed if the dreaded kala-azar were to be eventually eradicated.

Victoria's Taxi-Cab Ride

Prior to her trip to India and armed with a vision and conviction that she could make a difference, Victoria Hale had quit her job and began to investigate what it would take to establish the world's first non-profit pharmaceutical company (Hale, Woo, & Lipton 2005). It was now the summer of 2000 in New York City, and she sat in the back of a taxicab on her way to a consulting job she juggled at the same time. Victoria Hale was shaken to her core during that epiphanous taxi ride.

Intrigued by their quick and revealing stories, Victoria Hale loved talking to taxi cab drivers. Outgoing and curious about the world around her she noted that his name was 'Teremesha Maskini,' which was printed on the small placard in front of her. She asked him where he was originally from. 'West Africa,' he answered. Perking up even more, she asked about his name, Teremesha. 'It means 'always willing to serve the poor' in Nigerian,' he politely answered. Equally curious about her, Teremesha asked what she did for a living. Dr. Hale merely answered, 'I'm a pharmaceutical scientist.' Her answer was met with a loud, deep guffaw and the retort, 'You guys have all the money!' (Dusky 2007: 1).

Victoria and Ahvie Take a Stand

At that very moment, she realised it was true – and something had to be done. She spoke to her equally minded socially responsible husband. Now was the time to act. The couple hired a law firm to help them achieve the tax exemption necessary to create the unprecedented non-profit drug company. The multi-phase application process was a component of normal IRS procedures, which lasted more than ten-months (IRS 2010). The IRS raised questions as to the true nature of a non-profit pharmaceutical organisation through a series of questions. The couple was challenged to find an example of an existing non-profit that mirrored a for-profit business.

A few days later, while listening to a talk show it hit Victoria: National Public Radio (NPR) and public television. As a non-profit broadcast organisation, NPR operated much like their profit-based cousins, but they served a different listening audience with programmes their commercial broadcast counterparts did not provide, simply because such programming was unprofitable. Coincidentally, just two weeks later, the IRS approved the condition for the non-profit status of their pharmaceutical organisation. In July of 2000, Victoria and Ahvie developed their organisation calling it the Institute for OneWorld Health (iOWH), with the intent and purpose to develop paromomycin and battle the dreaded kala-azar (New York Times 2006).

In early 2001, armed with their 501(c) (3) non-profit status, Drs. Hale and Herskowitz were faced with the stark reality of funding their non-profit enterprise. Without an immediate outside source of funding, Victoria and Ahvie put up \$100,000 of their own money, and signed a \$315,000 promissory note. They also used the ground floor of their home as their office and worked without pay for two years (iOWH 2010a). They were now precariously prepared to match a neglected drug with one of the world's most onerous neglected diseases. The next step was convincing the World Health Organisation to turnover their Phase II data to iOWH in order to conduct the Phase III trials. This would prove to a challenge. The road ahead for Victoria and Ahvie was indeed much like the roads in Bihar, full of potholes and treacherous diversions.

Challenges with the World Health Organisation

Developing drugs, even those that are already on the shelf takes money, and lots of it. Clinical trials are not cheap, and they must be done right to meet the rigorous standards of the Food and Drug Administration (FDA), European Medicines Agency (EMA), and other country's regulatory agencies. Accordingly, in July of 2000, Dr. Hale and Herskowitz asked the World Health Organisation (WHO) to engage their circumstance and help them complete the phase three studies necessary to bring paromomycin to the Indian marketplace. However, the WHO was already working on another drug in partnership with Aeterna Zentaris, a small, for-profit pharmaceutical company, as well as the Indian government.

The drug under current review, miltefosine, had the advantage of oral administration. However, there are toxicities associated with miltefosine, which coincidentally is also used to treat cancer. The drug caused gastrointestinal side effects in one-third of patients, and is teratogenic (causing foetus malformations) in animals, thus requiring women of childbearing age to be prudent in the use of birth control. Further, close supervision is required during the 21-day course of therapy. In contrast, paromomycin had shown very limited side effects in trials. However, scientists at the WHO did not necessarily want to stretch limited resources between the development of miltefosine and paromomycin. After all, miltefosine was an effective anti-leishmania drug and it had the advantage of oral administration. However, at an anticipated price of \$100 to \$200 per treatment, miltefosine would be too expensive for most patients in developing countries to afford let alone purchase. At the time, it would be expected that any treatment would be too expensive. Yet, paromomycin would only be a fraction of that cost. The World Health Organisation was not immediately sold on adding paromomycin to their efforts. Initially they wanted to make sure their efforts to get miltefosine to the marketplace were not diverted before they committed to working with the Institute for OneWorld Health. In addition, of course, there was a funding issue.

Ongoing negotiations between Institute OneWorld Health, the World Health Organisation and the Bill and Melinda Gates Foundation proved to be the answer. The Gates Foundation believed in the development of technology as an important piece in helping to rid the world of neglected diseases. Therefore, in 2002, the Gates Foundation funded the first VL/paromomycin drug development project. Hence, in 2003, armed with some substantive funding, the Institute for OneWorld Health signed a licensing agreement with the Special Programme for Research and Training in Tropical Disease (TDR), which is part of the World Health Organisation (WHO), to develop a new cure for VL. Thus began the largest Phase III clinical trial for VL, all conducted in India.

Arguably, the Bill and Melinda Gates Foundation is the largest single contributor to Institute for OneWorld Health and other like-minded partnerships. There were other donors, like the Chiron Foundation and Sapling Foundation, which awarded grants in 2004 to study the VL among other treatments. However, their contributions,

while needed and appreciated, were small compared to the overall budget needed to advance paromomycin. By 2005, Institute for OneWorld Health and WHO/TDR completed the Phase III trial in India using paromomycin. Clinical cure was 94 per cent (Sundar et al. 2007). Moreover, in the same year, the Institute for OneWorld Health received another grant of US\$10 million from the Bill Gates Foundation for continued paromomycin production and distribution (iOWH 2010c).

INSTITUTE FOR ONEWORLD HEALTH (iOWH)

Based in San Francisco, California, the Institute for OneWorld Health (iOWH) is a leading non-profit pharmaceutical organisation that operates under a standard entrepreneurial business model. Its product development objective is to conduct limited R&D, although its primary focus is on production of drugs as well as vaccines for a variety of disease projects. The iOWH is charitably funded by the philanthropic efforts of the Bill & Melinda Gates Foundation (iOWH 2010c).

With nearly a decade of creating public-private partnerships (PPPs) and initiatives, iOWH has an extensive disease projects portfolio. The portfolios consist largely of tropical parasitic diseases including malaria, Chagas disease (also called American trypanosomiasis), schistosomiasis, and visceral leishmaniasis (VL). Rather than concentrating on new drug discoveries or heavily funding R&D, iOWH concentrates instead on drug development in particular those where it can structure licenses of late-stage development candidates. In 2005, iOWH completed Phase III trials of paromomycin sulphate (Kolaczinski et al 2008). Its therapeutic development resulted in a new therapy that could be used in a cure for the deadly VL (kala-azar) disease. In 2006, Paromomycin received approval by the Drug Controller General of India (Kolaczinski et al 2008).

The Institute for OneWorld Health identifies itself as a socially responsible organisation, one that measures its actions and decision-making based on a holistic approach to their bottom-line. Understanding that decisions made will affect stakeholders, iOWH operates with transparency when engaging suppliers, contractors, government entities and community leaders. Where in some circumstances corporate social responsibility (CSR) has become a manner by which organisations

manage, reduce or even avoid risk, in reality, CSR is an opportunity to create, generate, improve, and ultimately sustain performance for both people and the environment. For poverty-stricken areas like Bihar, iOWH has embraced CSR and defined it as an innovative partnership among NGOs, international labour organisations (ILOs) and intergovernmental organisations (IGOs) that engage a philanthropic approach to social health conditions.

Other pharmaceutical companies including BioDelivery Sciences, Gilead Sciences, Fujisawa Healthcare, AmBisome, and GlaxoSmithKline have launched clinical trials as well as oral formulation of liposomal (vesicle layers used to convey vaccines to target cells) (see Exhibit 6: Products in active development from preclinical to launched status). In 2007, GlaxoSmithKline (GSK) completed Phase II trials on their development of sitamaquine an oral monthly treatment compound¹³. GlaxoSmithKline's compound promises to be cost-effective for distribution in all high-risk regions (Kolaczinski et al. 2008).

While the eradication of leishmaniasis is but a dream, India's Ministry of Health estimated in 2002 that the elimination process would require 70,000 drug treatments per year to compromise the infection rate and be a deterrent to its endemic areas of Bihar and its border areas of Bangladesh and Nepal (Government of Bihar 2010). The Ministry of Health has hopes to engage and manage a distribution programme similar to leprosy and tuberculosis vaccine delivery systems through a number of public-private partnerships. Such a drug delivery system is suitable and integrated through primary healthcare clinics both private and public.

The Ministry of Health has utilised practical prevention measures to alleviate the spread of VL from animal to human without eradicating livestock or other animals such as dogs. Practical vector control measures include insecticide spraying and collars for dogs to control sandfly populations. Such efforts are intended to reduce rather than eliminate disease transmission. The poorest communities of the region have the highest probability of success with the collective effort of drug treatment and transmission reduction measures.

Paromomycin, Just In Time

By 2006, the Institute for OneWorld Health received approval for Paromomycin IM Injection (intramuscular, i.e. injection within the muscle) from the regulatory agency in India, the Drug Controller General of India (DCGI) for the treatment of visceral leishmaniasis (Government of Bihar 2010). Further, OneWorld Health brokered a partnership with Gland Pharma Limited, a family-owned profit-based Indian pharmaceutical company to manufacture and distribute the medicine at cost. Gland Pharma Limited Pharmaceuticals justified this move based on their desire to be socially responsible and to build pride with their employees (Interview Dr. Ahvie Herskowitz, October 15, 2010). After all, Gland was an Indian company and VL was largely an Indian disease (iOWH 2010d). 'At cost' equated to approximately US\$10 to \$15 per treatment course, which was significantly below the cost of other approved VL treatments. Additionally, Paromomycin IM Injection could be administered in clinic settings (Hale, Woo & Lipton 2005). While administration must be done daily over a 21-day period, ultimately it does not require hospitalisation, which was demonstrated later in a Phase IV study started in 2007 (Interview Dr. Ahvie Herskowitz, October 15, 2010). Most importantly, though side effects occur, these are primarily limited to redness and irritation at the injection site (Sundar et al. 2007). Consequently, this treatment management system proved to be hugely advantageous over previous standard treatments. By 2007, Paromomycin IM Injection was designated by the World Health Organisation (WHO) for inclusion on its list of Essential Medicines for developing countries (iOWH 2010b).

KALA-AZAR KNOCKED ON THE DOOR OF THE MISHRA FAMILY

It was March 15, 2007 and Sabal's fevers worried his mother. While fevers are prevalent in rural Bihar, they normally abate within a few days, yet Sabal's fever had lasted nearly a month. Sabal's fevers were not only persistent, now he was losing weight. Pakhi thought of her brother, Rajak, and shuddered. Could it be the dreaded and feared kala-azar? In 2007, the roads were only slightly better than the days her parents travelled to the clinic for Rajak's treatments in 1991. But Pakhi could no longer watch her child so weak and so young waste away. She talked to her husband,

who agreed they would make the five hour round trip to the visit the doctor at the nearest clinic. Pakhi's mother Dadi, elderly but strong, would stay with the younger children and watch their small farm.

At the clinic, a worried and caring young physician, Dr. Kumar, carefully examined Sabal. His blood was drawn. Quickly suspecting VL, he ran diagnostic tests to look for the telltale antibodies that would implicate the disease. After letting Pakhi and her husband know of the positive results, he quickly reassured them that there was an improved and affordable treatment now available from the Institute for OneWorld Health (iOWH) clinic nearby. The Mishra family was also told that the Institute for OneWorld Health could pay for their treatments, but they must come daily for the 21-day therapy. The family decided that Pakhi would make the daily commute to the iOWH clinic, using her husband's bicycle. Pakhi would gladly take on the taxing condition to avoid seeing her child die, as had her brother so many years before. For 21-days, she braved rain, wind, and occasional flooding to make sure her child had his daily injections. Slowly, Sabal began to respond. The fevers went away and Sabal began to have an appetite again. He started to gain weight. After his treatments were finished, Sabal had not only gained all the weight he had lost, but he had gained another five pounds and had grown another inch! Pakhi said her prayers and gave her thanks. Kala-azar had been defeated; it would not destroy her son or her family.

Ongoing Challenges

Although Sabal was saved, others impacted by the dreaded kala-azar may not be as fortunate. There are families impacted by VL who are even more remote than Sabal's family, and may not have the resources to make the trip into the iOWH clinics. Dr Herskowitz illustrated the challenge by relaying a conversation he had with a minister of health from another developing country. He asked that minister of health what his government could afford to pay for a drug that could eradicate a disease like visceral leishmaniasis. The Minister of Health replied, 'For free is too expensive' (Interview Dr. Ahvie Herskowitz, October 15, 2010). This underscores the enormous access and logistics problem in getting medicine to people in the developing world. Initially, the Indian government

stated that for families who could not afford the \$10 for paromomycin, they would provide the treatment free of cost (iOWH 2010c). The government of India has demonstrated strong support for eradicating VL, as evidenced by maintaining a national hospital and research centre (See Exhibit 7). However, as of 2009, the government of India had yet to approve paromomycin for use by the national public health programme. Consequently, additional bureaucratic hurdles seem to delay the distribution of paromomycin to the population in need.

Thousands of patients have been cured of VL through doses that have been given to Indians through the efforts of the Institute for OneWorld Health, their clinics, and the donations made by their funding partners. The Institute for OneWorld Health is an example of a unique public-private partnership, since it operates as a virtual pharmaceutical company by collaborating with clinical research, industry, manufacturing, and governmental agencies. However, as recently as 2008, virtually all their income was from non-profit organisations and 95 per cent was from the Bill & Melinda Gates Foundation (iOWH 2010c). Non-profit entities are reluctant to fund philanthropic endeavours forever (Hale, Woo, & Lipton 2005). Since drug development, securing governmental approvals, and then providing access to it in remote undeveloped areas is very expensive, it would behove the public-private partnership to find self-sustaining methods of funding without compromising their underlying core mission (Barr 2007). One method of doing this is to target disease states that have a market in both the developed world and the developing world, like tuberculosis, malaria, and HIV/AIDS (Widdus 2001). These are diseases that the public is more aware of and has sufferers in both developed and developing countries. Should these diseases take precedence since sustainable funding models may be easier to develop? Ideally, the public-private partnership can subsidise treatments and access costs in the third world by using profits generated in the developed world. Yet for neglected diseases, like visceral leishmaniasis, a market outside the developing world does not exist (Trouiller et al., 2002).

Pursuing treatments and cures for neglected diseases that are non-existent outside the developing world is a highly risky venture for a public-private partnership. By nature, they are an

altruistic organisation. Unlike their profit-oriented cousins, the pharmaceutical company, their goal is solely to reduce or stamp out disease, not make a profit. Ultimately, they can spend millions of dollars of philanthropic money and possibly fail. The philanthropy could have potentially invested their money in a different manner and achieved their goal of enhanced healthcare. Therefore, it is a risk for both the public-private partnership and its philanthropic funding partners. Just as there is no guarantee of success in any drug development project, profit-oriented or otherwise, there is no guarantee of success just because motives are considered noble.

VICTORIA CONTEMPLATES THE FUTURE

In 2008, leaving the reigns of iOWH in the capable hands of Dr. Richard Chin, Victoria pursued the enterprise of another non-profit pharmaceutical company. Medicines360 was established in early 2009 to serve the medical needs of women and children (Medicines360 2011a). Medicines360's mission is to focus on the development of products to treat the unmet needs of women and work toward self-sustainability through commercial sales revenue (Medicines360 2011b). While her experience founding the Institute for OneWorld Health taught her invaluable lessons in forming partnerships and the world's first non-profit pharmaceutical company, Victoria realised the effort to fight neglected diseases in developing countries was not sustainable without the continued generosity of philanthropic organisations combined with a country's financial support. In contrast, the principles behind Medicines360 would permit Victoria to develop a sustainable model that would offer affordable medical solutions for all women. The model is part of a social enterprise where profits from sales of products subsidise poor and marginalised women's medical needs (Medicines360 2011c). Unlike the unmet needs of visceral leishmaniasis, there is a viable market in the developed world for unmet contraceptive needs. The Medicines360 organisation would

give Victoria the opportunity to reach thousands of poverty-stricken women not only abroad, but also in the U.S.

Although no longer involved with the daily operations at iOWH, Victoria persevered in her vision to start the world's first non-profit pharmaceutical company. Nevertheless, Victoria's dedication and belief in a dream had been realised. That steadfast commitment culminated in thousands of Indians in Bihar State receiving the life-saving drug, paromomycin.

Yet the work was not finished. Many more in India needed treatment. Visceral leishmaniasis had sufferers in Nepal and Bangladesh as well. Access was inadequate and the infrastructure for medical support sketchy at best. To address these issues a Phase IV trial was conducted in India, which focused on the safety and efficacy of Paromomycin Injection in progressively more rural conditions in and around Bihar (Olliaro, Darley, Laxminarayan & Sundar 2009). Such trials are by practice planned as post-marketing studies of drugs, devices, or techniques that have been approved for general sale. These studies are often conducted to obtain additional data about a marketed product (Galson 2009). In essence, the Phase IV study sought to address adequately access issues in these rural areas to ascertain the most efficient means to develop an infrastructure to support a more robust outreach toward these populations. An innovative public private partnership model of an affordable programme dedicated to impoverished sufferers of VL was needed, not just in India but other countries where VL was endemic as well.

Much work had been done. Yet, much more work still lay ahead. And there were so many diseases and conditions among impoverished peoples around the world that needed to be addressed. Victoria worried about the process. Even so, in her heart she knew that indeed the innovative public-private partnerships that had established the world's first non-profit pharmaceutical company would bring the world one-step closer to the treatment and eradication of visceral leishmaniasis.

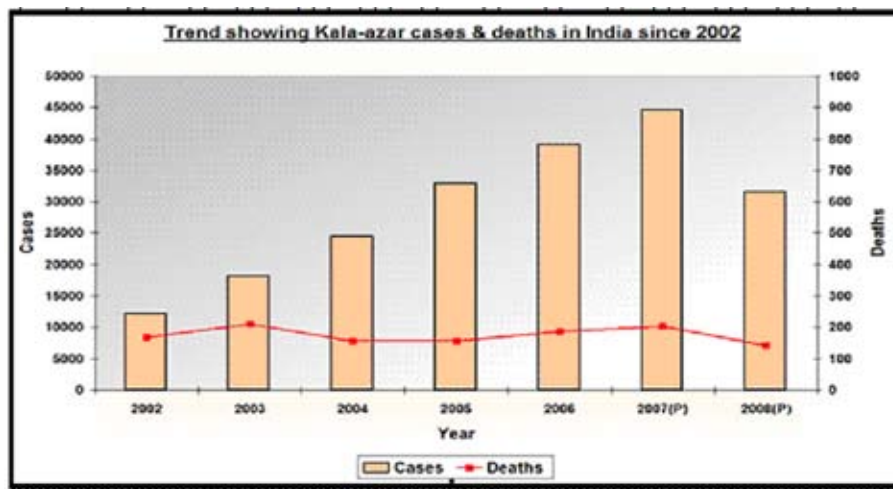
EXHIBITS

Exhibit 1: Countries where Leishmaniasis is Endemic



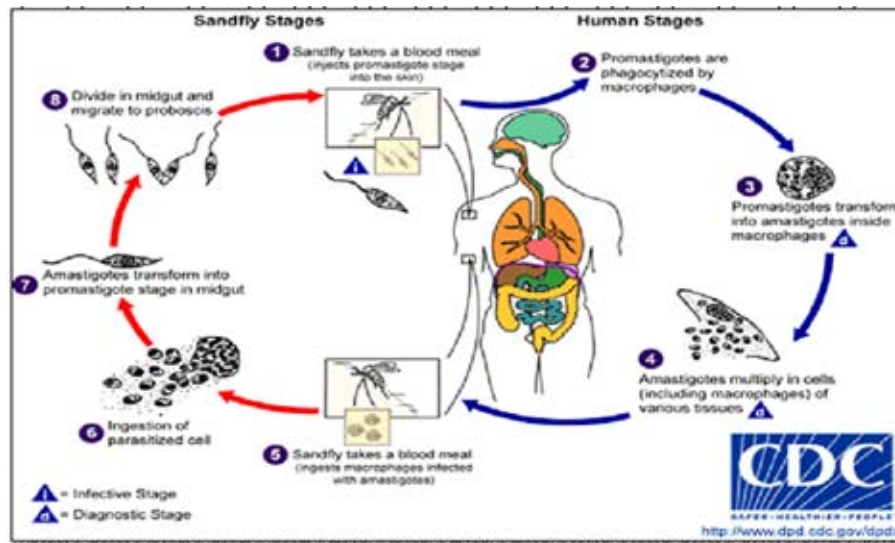
Source: B. David Company (2009) – Leishmaniasis Alert. Retrieved October 13, 2010 from <http://www.bdavidwater.com/mosquito-nets.html>

EXHIBIT 2: Kala-azar Cases and Deaths in India since 2002



Source: National Vector Borne Disease Control Programme: Ministry of Health & Family Welfare. Retrieved October 13, 2010, from <http://nvbdcp.gov.in/kala-azar.html>

Exhibit 3: Life Cycle of Leishmaniasis



Leishmaniasis is transmitted by the bite of female phlebotomine sandflies. The sandflies inject the infective stage, promastigotes, during blood meals. Promastigotes that reach the puncture wound are phagocytised by macrophages and transform into amastigotes. Amastigotes multiply in infected cells and affect different tissues, depending in part on the Leishmania species. This originates the clinical manifestations of leishmaniasis. Sandflies become infected during blood meals on an infected host when they ingest macrophages infected with amastigotes (). In the sandfly's midgut, the parasites differentiate into promastigotes, which multiply and migrate to the proboscis.

Source: Centres for Disease Control and Prevention Parasite and Health website. Retrieved October 13, 2010 from <http://www.dpd.cdc.gov/dpdx/HTML/Leishmaniasis.htm>

Exhibit 4: The State of Bihar at a Glance

State capital	Patna
Area	94,163.00 sq. km.
Area under forests	30,078.03 sq km
Latitude	21°-58'-10" ~ 27°-31'-15" N
Longitude	82°-19'-50" ~ 88°-17'-40" E
Altitude	173 Feet
Population (2001)	82,878,796
Population density	880 per sq km
Male population	43,153,964
Female population	39,724,832
Sex ratio	921
Literacy rate	47.53 per cent
No. of districts	38
No. of towns	130
Largest city	Patna
Languages spoken	Hindi, Urdu, Bhojpuri, Magahi, Maithili
Male population	26,898,918
Female population	25,951,644
Sex Ratio	965 females per 1000 males
Literacy rate	66.60 per cent
Per Capita Income (03-04)	Rs 21696
Religions	Hindus, Jains, Muslims, Christians
Language (s) spoken	Kannada, Telugu, Tamil, Hindi & English
Time zone	IST (UTC+5:30)
Temperature	Min. 5 °C; Max. 45 °C
Average Rainfall	1200 mm

Source: Government of Bihar Official Web Portal. Retrieved October 13, 2010 from <http://gov.bih.nic.in/Profile/default.htm>

Exhibit 5: Dr. Shyam Sundar Checks Rural Children for Kala-azar in Bihar State



Dr. Shyam Sundar checks rural children for signs of kala-azar (visceral leishmaniasis). The resurgent parasitic disease kills 200,000 people a year worldwide. The infection is fatal without treatment. Sundar runs a small, charitable kala-azar hospital in the district capital of Muzaffarpur.

Source: Photo by Geoffrey Cowley on the topic of Global Health used with permission from Photo Share contest winners. Retrieved October 13, 2010, <http://www.photoshare.org/contest/2005/05winners.php>

Exhibit 6: Products in Active Development from Preclinical to Launched Status

Generic Name	World Status	Originator	Primary Indication
amphotericin B, Gilead	Launched	Gilead Sciences	Infection, general
leishmaniasis vaccine, GSK	Phase I Clinical Trial	GlaxoSmithKline	Infection, leishmaniasis
miltefosine	Launched	AEterna Zentaris	Cancer, skin, general
sitamaquine	Phase II Clinical Trial	GlaxoSmithKline	Infection, leishmaniasis
aminosidine, iOWH	Registered	Institute for OneWorld Health	Infection, leishmaniasis
amphotericin B, BDSI	Preclinical	BioDelivery Sciences	Infection, leishmaniasis
leishmaniasis ther, Helix	Preclinical	Helix BioMedix	Infection, leishmaniasis

Source: PharmaProjects® - Pharmaceutical Research & Development Pipeline Intelligence United Kingdom. Retrieved October 13, 2010 from http://www.pharmaprojects.com/therapy_analysis/leishtable.htm

Exhibit 7: VL Hospital



Source: Photo provided and used with permission from Ahvie Herskowitz, M.D.

Exhibit 8: Doctor Sundar (left) with Dr. Thakur, Indian Minister of Health, and Victoria Hale (right) in Muzaffarpur, State of Bihar, India



Source: Photo printed by permission of Ahvie Herskowitz, M.D.

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INSTITUTE FOR ONE WORLD HEALTH (IOWH): SHAPING THE FUTURE WHEN LIFE IS HARD ENOUGH

INSTRUCTOR'S MANUAL

CASE SYNOPSIS

Five countries on three continents account for more than 90 per cent of all visceral leishmaniasis (VL) disease cases. Visceral leishmaniasis, commonly known as kala-azar or black fever, is a tropical parasitic disease. Affecting any age group, but often the very young, the disease presents its victims with intermittent fever, anaemia, enlarged spleen and liver and the gauntness of emaciation (Bhattacharya, Sur, & Karbwang 2006; Bora 1999). While north and east Brazil in South America, Sudan in Africa, and India, Bangladesh and Nepal in the Indian subcontinent comprise the majority of the cases, of these the north-eastern state of Bihar, India sustains the most serious public health crisis (Olliaro et al. 2005). Left untreated, VL will usually result in certain death. While there are treatments for this devastating disease, the parasite that causes VL has developed resistance to many antibiotics. In addition, these treatments are cost-prohibitive and require expensive hospitalisation over several weeks (Vanlergerghe et al. 2007). Poverty is the lead determinant of this insidious disease that is seemingly predisposed to affect poor populations who have little to no access to healthcare facilities nor can afford long-term treatment (Boelaert et al. 2009). New treatments are desperately needed to contain this disease.

This case chronicles an impoverished family in Bihar that has experienced the destructive effects of VL with neighbours and family. The family lives in fear for the health and wellbeing of their children. The case outlines the unique needs of a population affected by a neglected disease for which there is no market for a cure in the developed world, and therefore a lack of incentive to develop

an effective and cost-efficient treatment. Owing to her professional background in both public and private enterprises, along with her personal desire to make a difference, this case study also chronicles the inspirational brainchild of Victoria Hale, PhD, her husband, Ahvie Herskowitz, MD, the Institute of OneWorld Health (iOWH), and a relationship building of non-typical public-private partnership. This case highlights the need for a unique partnership, outlines the struggles in launching one, and the ensuing challenges faced in maintaining funding for a development project that will not see fruition for several years.

CASE ISSUES AND SUBJECTS

This case serves as an educational tool for discussing and understanding the subject of Public-Private Partnership and their ability to address unmet needs. The case is intended for both undergraduate and graduate courses in building alliances and creating coalitions. This type of case study is also applicable to courses in leadership in organisations and international management. It seeks to provide an applied, hands-on format to challenge students to increase understanding and integration into real world applications.

This case is further intended to examine organisations that embrace private and non-profit partnership as a fundamental organisational principle to promote collaborative efforts to treat visceral leishmaniasis (a parasitic disease) by providing low cost and effective medicines to households and healthcare systems in India.

INTENDED COURSES AND LEVELS

This case is intended for class study application of concepts learned in the classroom. This case is intended for undergraduate or graduate courses in Public-Private Partnership and Building Partnerships and Creating Coalitions. It is designed to complement knowledge derived from concepts in public and private partnerships. In other words, it seeks to provide an applied, hands-on format for students to increase their understanding of these topics. Answers to the questions in the case will derive from what students learned from theories and concepts.

CASE OBJECTIVES

The core pedagogical objective of the case is to help provide an applied, hands-on format for students to increase their understanding of the topics of Public-Private Partnership (PPP), building alliances, and creating coalitions among organisations.

More specifically, at the completion of this case the student will be able to:

1. Explain the principles and functions behind public-private partnership.
2. Understand the various types of collaborative structures available to organisations
3. Understand and explain the need for a public private partnership to address unmet needs in the global market place.

SUGGESTED CLASSROOM APPROACHES TO THE CASE

1. Introduction of the case in the class

It is recommended that the instructor introduce the script at least a week before the class discussions (duration from 30 minutes-1.00 hour) and assign the questions derived from the case. Doing so ensures that the students have read and understood the issues of the case. While this case could be done on an individual basis, the authors found it most effective to create case study groups and request formal group answers to the case questions. If it is to be done in a group environment, please refer

to groups' formation, report, and presentation for more teaching instructions.

While there is no one single approach to addressing ethics, social responsibility, and partnerships emphasising student application of such constructs is extremely important to the learning process. Individually or as a five-member group, students will be asked to discuss and answer the case questions. A PowerPoint presentation and a written report of 2-3 pages should address the case questions.

Based on the authors' experience, requiring a formal response to the questions to help students enhance their written communication skills is a good approach. Please note that this formal write-up of the case requires the instructor to read and grade the students' work more critically. Because of the nature of this case study, it is suggested that the class be divided into groups of up to five students per group. The students will read the case and respond to the questions as a group.

Answers to the questions in the case will derive from what students learned from the course concepts, textbook, and outside reading material. The case is to be completed and presented for class discussions.

2. Forming Groups

At least a week before the class discussions, students will be encouraged to network and get to know fellow students in order for them to decide with whom they want to team. Allow 10-15 minutes towards the end of the class meeting to submit group members' names. Initially, students need to form a group of up to five students to conduct this required study.

3. Process

Each group will start working on this case after the instructor introduces the subjects of ethics and social responsibility. In a group setting, students are expected to develop and build their responses based on their acquired knowledge. It is recommended that the instructor address and clarify case questions.

4. Use of PowerPoint and Audiovisuals

It is recommended that students be encouraged to create an effective group presentation. This could be achieved utilising audio-visual materials, including but not limited to PowerPoint. The case itself does not come with a video. However, several YouTube videos outline the challenges and attempts to eradicate the disease. For example, the videos entitled "Dr. Shyam Sundar – Treatment of Visceral Leishmaniasis in Indian Subcontinent" or "Leishmaniasis – India" represent a quick review and introduction to VL.

5. Group Report and Presentation

Each group is required to write at least a 2-3 page report (12-point font, double-spaced and using the APA writing format). One report is needed for each group. Each group is also required to prepare a 10-15 minute PowerPoint presentation explaining its answers. Students are required to use the chapters assigned for the course. To support their responses and enhance their report, students must include outside references such as books, journals, newspapers, internet information, or a direct interview as resources for the case answers (in case of an interview, they need to include the interview questions as an appendix of the report).

6. Recommended Outline

The structure of the written report is critical. In the first part of the case write-up, students should provide salient points of the case before proceeding to answering the case questions.

In the second part of the case write-up, students present their answers and recommendations. Instructors need to encourage them to be comprehensive in their answers, and make sure that answers are in line with the previous ones so that it fits together and moves logically from one to the next.

7. Starting the Class Discussion

Before engaging in a class case discussion and presentations, it is recommended to stress to the students that they might be disagreeing with the points that are being made by other students and that this disagreement is healthy and should not be taken personally. A reminder is helpful.

This clarification and reminder ensures that the disagreements/discussions remain open and inviting and do not turn into personal matters.

8. Analysis

Since this case is an application of topics covered in the subjects of organisational ethics and social responsibility, students' understanding of these concepts will be essential.

9. Content and Grading

Students' answers and presentations should clearly and concisely demonstrate their knowledge and comprehension of the subject concepts learned in the class, as well as the individual or the group's ability to apply knowledge learned in class and through research (synthesise, analyse, and evaluate his/her/their work). Students will be graded based on the following criteria: (a) The use of innovative and creative ideas, (b) the application of concepts learned in the class, and (c) the use of outside research to support the case.

It is recommended that this case study constitute 15-20 per cent of the student's participation grade.

RESEARCH METHODOLOGY AND EXPERIENCE TEACHING WITH THE CASE

1. Research Methodology

This research is based on published secondary data and some interviews obtained by the authors from available sources related to the case.

2. Experience Teaching with the Case

One of the authors has used "Institute for OneWorld Health (iOWH): Shaping the Future When Life is Hard" case in a graduate course "Building Partnerships and Creating Coalitions" and in a undergraduate course "Introduction to Public Administration." The instructor applied the case after covering the course related subjects of Public Private Partnerships. The case was well received by students.

DISCUSSION QUESTIONS

1. What factors of a public-private partnership are demonstrated in this case study?

Public-private partnerships (PPP) exist in a myriad of complex structures. In this context, a PPP is defined as a strategic initiative between two or more parties with the goal to develop a successful, long term, strategic relationship to achieve best practices for sustainable healthcare treatment in the developing world. In the past forty years, PPPs have evolved from minimally collaborative associations to completely forged and fully endorsed organisations. Exhibit 1 exemplifies the shift from minimal integration between organisations to full-scale collaborations among a number of agencies both public and private. Students will need to identify the particular public-private partnership relating to healthcare delivery systems. Additionally, students will describe how such a relationship presented the opportunity to provide drugs and vaccines for infectious diseases to developing nations.

Such public/private joint ventures further require funding, which can be an obstacle preventing adequate and sustained financial support. Students can explore partnership relations between non-government organisations (NGOs) and non-profit organisations such as the Gates Foundation discussed in this case. However, identifying the specific collaboration and alliance with the Indian government (public), the World Health Organisation (NGOs), and Gland Pharmaceuticals (private) rendered a successful outcome, but such is not the case in other countries. Comparing outcomes between countries can be useful in determining positional risks and external factors that influence the success of public-private partnerships.

Since the 1990s PPP for healthcare have emerged with a primary goal to mitigate diseases in the developing world. Such partnerships have funded substantial R&D of a number of drugs, which have successfully been utilised in many countries including West Africa and Brazil. For example, drug development collaborations have achieved significant health improvement impacts such as the elimination of lymphatic filariasis (LF) in West Africa. Along with VL, lymphatic filariasis is another parasitic disease, which is considered

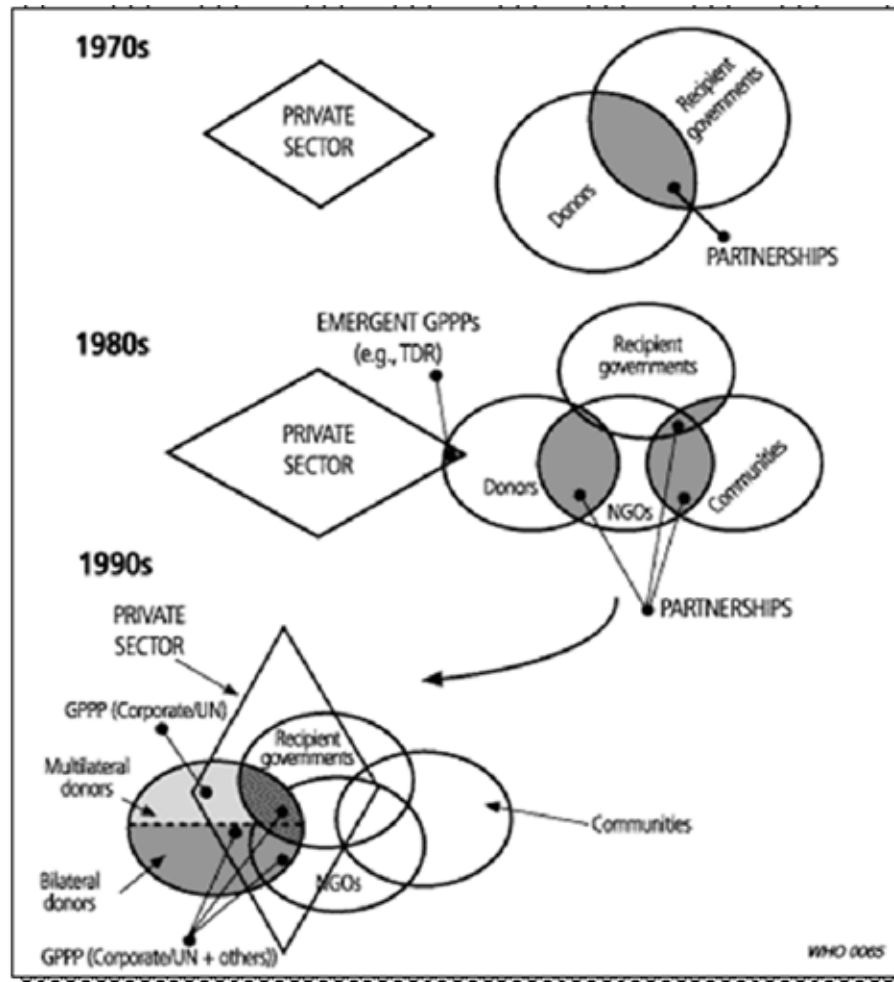
one of the six potentially eradicable diseases and malaria. Lymphatic filariasis causes elephantiasis, which is the thickening of the skin and underlying tissues (CDC 2010). Reaching millions of people in Africa and India, such partnerships have proven to be successful in either mitigation or elimination of neglected disease. Such partnerships have significant advantages that permit the ability for philanthropist organisations, pharmaceutical, and NGOs to pool their financial and knowledge management resources to deliver medicines through a pipeline of government delivery systems. While advantages do indeed exist, disadvantages such as liability can create conditions for externalities to influence or detract the partnership. Exhibit 2 is a basic chart that indicates partnership pros and cons. Students can use these as a foundation to breakdown individual factors and discuss specifics for iOWH.

2. Given the socio-economic conditions in the State of Bihar, what elements of the iOWH-WHO-Gland partnership were beneficial to cultivating change toward the Indian healthcare system?

Despite reservations due to government infrastructures, the leadership of Drs. Hale and Herskowitz focused on moving the project forward. The organisation was aware of the challenges they had which had to involve key stakeholders, to generate funds, manage the process effectively, and develop a viable product.

At the onset, the biggest challenge was the nature of the conditions for the delivery of VL treatment drugs and the period in which the goal was to be accomplished. Certainly, there seemed to be no way the organisation as going to get a consensus from the various stakeholders to generate sufficient product. However, the doctors were determined to succeed regardless of the financial and infrastructure conditions. An initial challenge was to provide a structure for the distribution process by developing a project management team. This is an essential factor in any partnership venture. Besides pulling together a task force, iOWH along with its partners had to determine roles and objectives each had to be responsible for and how to structure work within those roles to accomplish their objectives. Exhibit 3 is a Partnership team table indicating the team roles and objectives.

Exhibit 1: Paradigm Shift of Private and Public Relationships



Source: Global public-private partnerships: Part 1 a new development in health from the Bulletin of the World Health Organisation (Buse & Walt 2000).

Exhibit 2: Partnership Pros and Cons

Advantages	Disadvantages
Ability to pool financial resources	Unlimited liability (liable for mistakes)
Ability to share responsibility and capitalise on complementary skills	Potential for disagreements – drafted agreements can specify how disputes are resolved
Ease of formation	Difficulty in withdrawing from a partnership (some contracts are binding)
Possible tax advantage (avoids double taxation)	Lack of continuity Changes in ownership Addition or subtraction of partners

Source: Instructor designed table used in course presentations

Exhibit 3: Partnership Team Roles and Objectives

<i>Task Force Group</i>	<i>Roles & objectives</i>
Financial team	<p>Estimate the cost of implementing R&D, clinical trials, and delivery costs, in addition to full implementation of the delivery system within the State of Bihar</p> <p>Recommend and advise short and long term funding strategies including endowments, grants, and other sources to implement and sustain product manufacturing and delivery</p>
Clinical team	<p>Identify key barriers to the implementation of delivery systems and provide recommendations to mitigate potential barriers</p> <p>Develop criteria to prioritise between drug development and clinical trials and provide factual examples to support or substantiate drug product and type.</p> <p>Identify the types of communication exchange challenges that will be faced given the limited Indian infrastructure.</p> <p>Determine key medical delivery systems and groups that will enable healthcare delivery in designated areas.</p>
Governance team	<p>Draft a mission and vision statement that will permit collaborative processing of drug manufacturing, delivery, and treatment based on a set of guiding principles or ideology.</p> <p>Propose a governance model for implementing the system and develop a communication plan to sustain the project through the implementation phase</p>
Legal team	<p>Identify real and perceived legal barriers to a healthcare delivery system for both drug and medical staff</p> <p>Specifically address legal issues related to the product development generated by the clinical team.</p>

Source: Adapted from Harvard Business School Case (Applegate, Vinze, Raghu & Ipe 2009).

3. Based on the context of this case study will the private-public partnership created for the delivery of paromomycin treatment be successful in accomplishing the mission identified? Explain.

The mission, as identified in the case study, was eradication of visceral leishmaniasis. In answering this question, the student should know that to date VL has not been eradicated in afflicted regions, although many thousands of people have undergone successful treatment. To ascertain an assessment of eventual success, the student should be able to support their position by identifying that the elimination of VL is dependent on three successful initiatives:

- Providing effective and safe medications and treatment modalities
- Environmental abatement programmes aimed at reducing behaviours that promote human contact with the sandfly as well as the management of sandfly populations.
- Improving access to healthcare and long-term treatment for afflicted, impoverished populations

Student should determine that these three approaches to eradicate VL also require a sustainable fiscal model to finance continual implementation cost. As explained on page 14 of the case “non-profit entities are reluctant to fund philanthropic endeavours forever.” This particular case was largely dependent upon the continued generosity of the Bill and Melinda Gates Foundation. Thus, students need to analyse the potential outcomes and strategies needed should such foundational contributions wither or vanish. With such potential obstacles, students should investigate alternative funding mechanisms or other partnerships that could sustain the programme prior to the eventual eradication of the disease. Consider the possibility should conditions revert to increased cases of VL occurrences and more deaths.

Given that government is responsible for the health and welfare of its citizens in many of these third world countries, governments with such disease conditions are generally fully accountable for providing funding. However, Buse and Waxman (2001) suggest that in some cases partnerships

between private and governmental entities enable nations to relinquish their responsibilities for the protection of their citizens’ health. Students should be able to identify that in order for partnership to be effective, all parties, including governments, must be fully committed to the mission financially as well as philosophically. Governing bodies must ensure adequate and continual representation with partner NGOs or private institutions to ensure transparency, thus motivating acceptance and alleviating divergence of mission goals (Buse & Waxman 2001). Governance requirements of partnerships involving the World Health Organisation are listed in Exhibit 4:

Students should be able to articulate that an indecisive coalition of pharmaceutical companies involving donations to philanthropic organisations would not alone be adequate in any quest to eradicate VL. Consensus within the public-private partnership literature indicates that neither public organisations nor strictly public organisations are in the best position to tackle the complexities of global health care needs. Barr (2007) maintains such complexities will undoubtedly require a diverse and complex blend of system to battle global health care issues.

Further, successful outcomes will depend on the ability of public-private partnerships to be accountable for fiscal fortitude and organisational action outcomes. As such, each independent organisation committed to the partnership must replicate these same accountable factors. Moreover, because these types of partnerships are global relationships, each is subject to global public scrutiny and regulatory responsibility given the many crossed borders. Thus, maximising operational transparency and investing in clear public communication to clarify approaches and actions are crucial to such partnerships receiving validation and public support (Wheeler & Berkley 2001).

Exhibit 4: Governance Requirements

Partnerships with the World Health Organisation (WHO) should:

- Be governed by bodies that are widely representative yet give the WHO adequate decision-making power to reflect its position as the premier health organisation with universal representation. Moreover, the governing bodies should have mechanisms ensuring the participation of constituencies that might otherwise lack the material resources needed in order to participate, particularly those that provide a counterbalance to the influence of industry. All members should undertake to achieve to WHO principles.
- Establish clear goals, roles, responsibilities, and decision-making structures, and the means of monitoring and enforcing decisions should be taken into consideration
- Establish systems of communication whereby information about decision-making structures, funding, resource allocation and results is regularly conveyed to all concerned, and should provide for consultation with stakeholders.
- Document and publicise details of the process and outcomes of the partnership.

Source: Buse and Waxman (2001) Public-Private Health Partnerships: A Strategy for the World Health Organisation

1. Discuss the implications of the statement “Free is too expensive.” What are some of the challenges facing free drug distribution in rural areas? What suggestions can be made to adequately address these challenges?

Access and distribution are key terms students should be able to identify in discussing the implications of the statement “free is too expensive.” Gland Pharma Limited in India, a profit-based pharmaceutical company, agreed to make and sell paromomycin at their cost, which was only a \$10 per treatment course. Gland Pharma justified this move based on their mission that included a corporate social responsibility initiative to be global leaders for generic drugs deliverable to local communities. While, the drug was not “free,” per se it was priced considerably less than other medications available and in use. However, even with this nominal cost, the programme still needed to finance trained staff to administer the drug over the 21-day treatment period, finance the clinics, and further provide access to people in remote areas who are not likely to have the resources, transportation, or the ability to make the arduous trip to city clinics. Financing a health care delivery programme in impoverished areas of developing

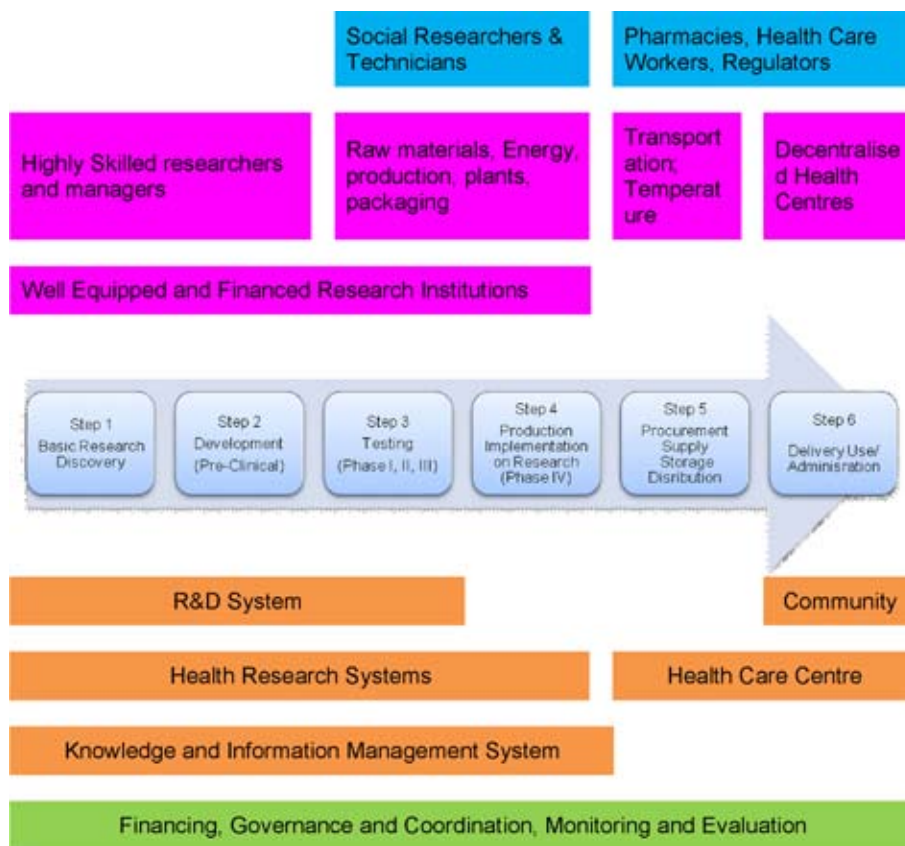
nations is a consequence and indeed an obstacle for obtaining free or low-cost medications. Therefore, while the cost of the drug is reasonable, a viable and sustainable financial model is crucial to deliver the drug to the target population.

Donation programmes that provide free medication, even those that are relatively non-controversial, have unintended consequences. Once a country receives donated or free medicine, government inadvertently incurs the financial burden to contract and deliver treatment. In rural areas, no viable infrastructure such as navigable roads exist, making delivery difficult. In addition, countries face issues with equity, since multiple areas or districts may be in dire need, yet donated product and the resources required to ensure access are limited (Buse & Waxman 2001). Indeed, as outlined in this case, the Indian government, while fully intending to provide the treatment free of cost, has yet to purchase one dose of paromomycin for its population (Schlein 2009). The question is not commitment, as demonstrated by India’s strong support in maintaining a kala-azar hospital and research centre, but one of sustaining a viable budget and financing.

Potential Solutions: Considering the case study issues and obstacles, students can attempt to

outline theoretical models to address access and delivery challenges. This case noted the iOWH Phase IV study, which sought to examine the safety and efficacy of paromomycin injection in progressively more rural conditions in and around Bihar. In essence, the Phase IV study sought to address access issues in these rural areas to adequately address what the most efficient means would be to develop and support a feasible infrastructure. Exhibit 5 is a visual map of “building blocks” that can help the instructor guide students in considering the issues that exists postproduction with procurement, supply, storage, distribution, delivery and use, and where they fit in the continuum for drug development and delivery:

Exhibit 5: Visual Mapping of Building Blocks for Drug Delivery



Source: Adapted from NEPAD-COHRED 2009 report on designing strategies for national pharmaceutical innovation

Focusing on steps (5) and (6) in the above visual map, the instructor can assist the student in understanding critical success factors in delivering medicines in impoverished rural areas of developing countries.

Finally, financing every aspect of drug development through delivery is an extremely difficult prospect especially for neglected diseases for which a profitable market does not exist. However, the World Health Organisation's Expert Working Group has developed an innovative set of proposals for financing sources, some of which are summarised in Exhibit 6(WHO 2010a).

These proposals are just a few fundraising mechanisms that can provide balance between the need to develop revenue and the disbursement of health care funds to serve those who cannot possibly afford VL or any disease treatment. These mechanisms are linked to allocating funds in a streamlined and effective manner. However, decisions to such funding alternatives are evaluated and applied through the public-private partnerships between the national government and the philanthropic organisation seeking to provide disease treatment programmes. Nevertheless, the allocation of earmarked funds must be applied transparently through effective and efficient fund disbursement mechanisms.

1. What may be some of the challenges faced by partnerships between profit and non-profit organisations? List challenges and provide an explanation.

Goal conflict between profit and non-profit partnerships: One of the challenges is that the primary motive or overarching goal of profit oriented vs. non-profit organisations can differ substantially. While both organisations may want to see a disease eradicated, the primary goal of a profit-oriented company is to do so while creating a profit for their organisation, employees, and other stakeholders. A certain amount of transparency and agreement up front is necessary to avoid hidden agendas and differing expectations. Both the profit oriented and non-profit organisation needed to realise and respect the value expected by their partners, and work toward their partner's value-platform without compromising their own.

Managing and setting expectations for the partnership: In order to successfully manage any partnership, considerable attention must be given to managing the relationship, which requires continuing communication. Parties need to define what the relationship means and agree to support each other's goals. Once it has been assessed that the relationship fit works, it must be not only managed, but also audited to ensure stated goals are being attained without compromising either party's objectives, making adjustments as necessary (Bamford, Gomes-Casseres & Robinson 2003).

An example of a potential conflict that was overcome included the partnership between iOWH and the World Health Organisation (WHO). While both are non-profits, they have different agendas for drug development. The World Health Organisation was developing mirtazipine for VL and initially did not want to dilute time and resources by working with iOWH toward the development of paromomycin. However, through careful negotiations and addressing funding issues, the WHO was able to see that developing both drugs in effect would "hedge their bets." Antibiotics develop resistance over time, and often can be synergistic when used together. Developing different treatment modalities for VL served the larger good, and complimented both the iOWH and the WHO's overarching goal of eradicating VL.

By the early 1980s, public policy and attitudes toward public-private relationships began to change. As non-profits re-examined their ideologies and influences, donor agencies began to channel funds through NGOs such as the WHO. Such joint ventures between agencies and NGOs resulted in explorations of ways to link profit based industry and the public sector to deliver healthcare in developing countries.

Since 1987, the WHO has collaborated with a number of pharmaceutical, NGOs, and private funding organisations to deliver drugs and vaccines in countries most in need of healthcare delivery. Seeking to mitigate or eliminate certain diseases some partnerships produced a number of joint ventures to combat or eliminate particular diseases. Exhibit 7 is an example of successful product-based healthcare public-private partnerships, each of which achieved set goals

Exhibit 6: Proposals for Financing

Positional Financing Approaches	
A new indirect tax (consumer based)	—These are small taxes imposed on specified products or transactions. Such a tax that is global in scope allows developing countries to contribute to fund-raising
Voluntary contributions from businesses and consumers	<p>—This approach involves voluntary donations by individual consumers. It can operate in one of three ways:</p> <ul style="list-style-type: none"> voluntary linking of a donation to payment for a service (e.g. payment of mobile phone bills or income tax); automatic donations directly to a particular recipient or voluntary but non-automatic donations (e.g. private giving campaign or endowment) <p>—An income tax donation allows an individual to contribute from his or her income, which the government matches with the income tax that would have been paid.</p> <p>—Voluntary business contributions are donations from the business sector as a share of its revenue or of its profits for charitable causes, or pro bono in-kind support to charitable activities. In return, the business earns good will, which may lead to extra sales and profits, or it may act more altruistically in the context of corporate social responsibility. Voluntary contributions are less certain funding streams than taxes, but, once established, they are reasonably predictable</p>
Taxation of repatriated pharmaceutical industry profits	—For example, governments would tax non-domestic pharmaceutical companies that undertake activities on their territories. The tax would be on all profits remitted to the overseas parent company.
New donor funds for health research, development	<p>—New donor approaches has three forms: (1) seek new or non-traditional donors national donors such as China and Venezuela; (2) existing donors that earmark a percentage of GDP for health R&D; (3) other philanthropic organisations</p> <p>—These fund-raising mechanisms could provide a balance between the consumer, governments and pharmaceutical industry; Voluntary and non-voluntary contributions; and Developing and developed country contributions</p>

Source: World Health Organisation (WHO) (2010b); Research and Development: Coordination and Financing, a Report of the Expert Working Group

Exhibit 7: Examples of Product-based health PPP

Name/Date	Partners	Goal	Scope
Mectizan® Donation Programme/ 1987	Merck & Co. WHO World Bank Task Force on Child Survival and Development National authorities and NGOs	To eliminate river blindness by treating everyone who needs it with Mectizan.	Drug donated until no longer required All 34 endemic countries have at some time been provided with free Mectizan Cumulative value of donation is estimated as US\$ 500 million. An additional US\$ 200 000 per year is spent on shipping plus the cost of the Mectizan Expert Committee and its Secretariat
Malarone® Donation Programme/1996	Glaxo Wellcome Task force on Child Survival and Development Medical Research Council, England National Institutes of Health, USA Centres for Diseases Control, Atlanta WHO World Bank Wellcome Trust National Authorities	To help combat drug-resistant malaria in endemic countries where cost often limits access to new drugs	Up to 1 million free doses per year globally through a targeted donation programme Plot donations in Kenya and Uganda
Albendazole Donation Programme/ 1998	WHO/Division of Control of Tropical Diseases SmithKline Beecham Global Programme to Eliminate Filariasis National authorities and NGOs	To accelerate the effort to eliminate lymphatic filariasis	Donation of albendazole to governments and other service providers until elephantiasis is eliminated The value of the donation of up to 6 billion doses over 20 years is over US\$ 1 billion
Zithromax® Donation Programme/ 1998	Pfizer Inc. E M Clark foundation Conrad H Hilton Foundation Bill and Melinda Gates Foundation Helen Keller International International Trachoma Initiative GET 2020 (WHO Alliance for Global Elimination of	To advance the global effort to eliminate blinding trachoma	Two year partnership (in the first instance) Donation of Zithromax by Pfizer valued at US\$ 60 million Pfizer and Edna Mc Connell Clark Foundation each providing US\$ 3.2 million to international Trachoma Initiative Five of 16 WHO priority countries included (Ghana,

Source: Global Public–Private Partnerships: A new development in health from the Bulletin of the World Health Organisation (Buse & Walt 2000).

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E-GOVERNMENT AND PUBLIC E-SERVICES IN ALBANIA. TRENDS AND CHALLENGES

ELSA GEGA
FACULTY OF ECONOMY AND LAW

ILIR ELMAZI
FINANCIAL AND ECONOMIC DIRECTOR OF SIGMA INSURANCE COMPANY, ALBANIA

Abstract

In Albania there is an emerging research on public e-Services and research is conducted at several universities and research institutes. Albanian research on e-Services focuses on citizens, communication, the development of e-Services, the design of e-Services, the maintenance of e-Services, e-Participation, the quality of services, evaluation, organizational changes, interactions between different e-Services, usability, co-operation, inter-organizational co-operation, accessibility, the development of methods, and process orientation. The purpose of this article is to increase the understanding of current research and to identify areas of co-operation and interest for further research. The following research questions are of interest. (1) What does current research concerning e-Government services focusing on? (2) What are the trends and visions for the area?; and (3) In what way does current Albanian research comply with international research, and trends and visions expressed for the future development and usage of public e- Services?

This paper is based on primary and secondary data. Primary data are results of a survey study on universities and higher education institutions that are entitled to offer postgraduate programs and also to research institutes in Albania. Secondary data are results of literature review and other studies in this field. The study was conducted during the spring and summer of 2010. To further increase the understanding of current research and to identify areas of co-operation and interest for further research, and also to provide a summarized picture of current research

in the field, the results of the survey study were further analyzed, assessed, and categorized. The analysis was based on the conception of e-Services. For this study, services in the context of contact between citizens or other stakeholders and government agencies or municipalities by means of information and communication technology (ICT) were examined. The contacts concern services from the government agencies to stakeholders as well as stakeholder potential to conduct a dialogue with a government agency.

Keywords: Public e-Services, e-Government, Public Information Systems.

1. Introduction

Electronic Government, or e-Government, with its many synonyms, is a growing field of practice and research all over the world [Grönlund and Horan, 2005; Grönlund, 2004; Scholl, 2004; Bruecher et. al, 2004; Bhatnagar, 2004]. E-Government in this context encompasses a wide range of branches and sub-areas, for example the dissemination of information, services to individual citizens and businesses and participatory democracy. According to Wimmer [2006], e-Government is multidisciplinary and consists of several domains of research and implementations as for example e-Democracy, e-Participation, e-Administration, e-Health, and e-Justice.

In the field of e-Government it has been emphasised that an important goal of e- Government is the delivery of faster and cheaper services and information to citizens, business partners, employees, other agencies, and government

agencies [Layne and Lee, 2001] and therefore, this article mainly focuses on public e-Services. There are currently many research efforts and development projects on e-Services in progress [Grönlund and Andersson, 2006; Lindblad-Gidlund and Löfstedt, 2006; Löfstedt, 2005], and there are several different types of actors in the development of e-Services, e.g. researchers from different disciplines, practitioners, and businesses. However, the problem of today seems to be insufficient awareness of the research that is under way, and who the actors are, and accordingly the research efforts are not efficiently coordinated and needs and requirements are not being observed. There has not been a good outline of current research in the area and there are several actors who claim that to encourage the research process and development of fully functional e-Government 2003a; 2003b; Dittrich et al., 2004, Vinnova, 2006a; Vinnova 2006b; Lindblad- Gidlund and Löfstedt, 2006].

Hence, the purpose of this article is to increase the understanding of current research and to identify areas of co-operation and interest for further research. The following research questions are of interest. (1) What does current research concerning e-Government services focusing on?; (2) What are the trends and visions for the area?; and (3) In what way does current Albanian research and Kosovo research comply with international research, and trends and visions expressed for the future development and usage of public e- Services?

2. Method

The launching platform for this research is a survey study on universities and higher education institutions that are entitled to offer postgraduate programmes and also to research institutes in Albania. The study was conducted during the spring and summer of 2009. To further increase the understanding of current research and to identify areas of co-operation and interest for further research, and also to provide a summarized picture of current research in the field, the results of the survey study were further analyzed, assessed, and categorized. The analysis was based on the conception of e-Services. For this study, services in the context of contact between citizens or other stakeholders and government agencies or municipalities by means of information and communication technology (ICT) were

examined. The contacts concern services from the government agencies to stakeholders as well as stakeholder potential to conduct a dialogue with a government agency.

The research found was first categorized based on the classification of the EU (2006a). According to the EU, e-Services can be divided into e-Services for e-Government and e-Services, and accordingly the research projects found were grouped according to this classification. Second, the research projects identified were grouped according to research focus and direction, i.e. if the research was at national or local governmental level. Third, the researchers were analyzed according to number of current projects, established collaboration, and number of publications.

To see to what degree the research corresponds to international research in terms of focus, research type, collaboration, and references, a comparison was made of a recent study conducted by Grönlund and Andersson [2006]. Furthermore, to be able to analyze the direction of the research and to see to what degree current research corresponds to needs, i.e. if it is governed by requirements, and to analyze important directions, focus, and type, the research identified was compared to trends and visions expressed by different actors [Albinsson et al., 2006; Nordfors et al., 2006; Skarin,

3. Current Research Concerning Public E-Services in Albania

Research on e-Services is conducted at several universities and research institutes in Albania. The EU [2006a] classifies e-services into two overarching groups, i.e. e- Services concerning e-Government and e-Services concerning e-Health. There were 32 research projects identified in the study. However, 23 research projects were considered not applicable to the analysis because of their direction or because information on them was too brief.

The classification of the EU [2006a] forms the basis for the classification and presentation of the research projects presented below. However, the result of the survey study indicates that current Albanian research on e-Services focuses on citizens, communication, the development of e-Services, the design of e-Services, the maintenance of e-Services, e-participation, the

quality of services, evaluation, organisational changes, interactions between different e-Services, usability, cooperation, inter-organisational cooperation, accessibility, e-Health, the development of methods, and process orientation.

3.1. Focus

Research on e-Services focuses on different levels of governments. The research also focuses on, e.g. governments, citizens or enterprises. Table 1 below presents the focus of current research in Albania and Kosovo.

As seen in Table 1, the focus of projects on e-Services vary. To provide a more detailed picture of current research projects in Albania, Table 2 below presents the focus and direction for both categories, i.e. the level of government agencies and the direction for each research projects on e-Government according to the definition by the EU [2006a].

3.2. Active Researchers

There were 61 researchers active in research on e-Services. The researchers identified in the study work at 21 universities, state university colleges, independent higher education institutions, or independent programme providers that are entitled to offer undergraduate programmes, and research institutes from our countries.

Almost every one of the universities and research institutes collaborated with other actors in the subject area in their research projects concerning e-Services. Some universities or research institutes collaborated with both national and international actors, whereas others cooperated with some or a few other Albanian and Kosovan universities or research institutes.

3.3. Publications

Researchers in the area of e-Services in Albania have produced numerous papers, reports, theses

and other contributions in the field. Table 2, below, gives a rough picture of references.

4. Albanian Research Compared to International Research

There are several tentative definitions of the concept of e-Government (see., e.g., [Bekkers and Homburg, 2007; Grönlund, 2004; Bathnagar, 2004; Curtin et al., 2004; COM 2003/567; Scholl, 2003; Marche and McNiven, 2003; Zweers and Planqué, 2001; Silcock, 2001; Hirst and Norton, 1998]) and in several definitions e-Services is a part of the definition. The interpretation of the concept by those participating in the study reveals that there is a prevailing varied understanding of the notion. In Albania research on e-Services is conducted at departments of different affiliations and this also substantiates the interdisciplinary of the research area. Furthermore, the conception of e-Services is closely connected to other conceptions in the area of e-Government, and the different parts border on each other. The structure of research organisations at the different seats of learning in Albania also confirms the interdisciplinary of the research area. The research is conducted at departments of different subject affiliations and moreover, some of the universities and research institutes have a research organisation structure with researchers from different disciplines. The research identified in the survey substantiates the opinion of Scholl [2004]. According to him, the complex relationship between information technology and government has become a major focus of academic research in several fields such as public administration, organisational behaviour, information science, and technology innovation. Thus, researchers who have chosen e-Government as a problem domain might have their starting point in several other disciplines, e.g. organisation theory, social science, informatics, computer science, public administration, business administration, economy, political science, law, government professionals, library science, etc.

Table 1. Research focus.

Research focus	nr	percent
E - government		
Focus on national governments	21	27%
Focus on local governments	10	12%
Focus on both national and local	7	9%
Focus unspecified	20	25%
Governmental focus	24	30%
Focus on citizens	5	6%
Focus on enterprises	2	3%
Focus on both governments and citizens	11	14%
Focus on both governments and enterprises	3	4%
Focus unspecified	13	16%
E-Health		
Focus on e-Health	2	3%

Table 2. Focus of research projects concerning e-Services

Research focus in research projects concerning e- services				
	National	Local	National+ Local	Unspecified
Governments	10	5	3	6
Citizens	3	-	1	1
Enterprises	-	-	1	1
Governments + Citizens	3	4	2	-
Governments + Enterprises	5	1	-	-
Unspecified	-	-	-	12

Table 3. Collaboration

<i>Collaboration</i>	Nr	Percent
<i>University – University</i>	9	41%
National and International	7	32%
National	1	5%
International	8	36%
<i>University – Governments</i>		
<i>University – Business</i>		
National and International	3	17%
National	7	32%
International	1	5%
Not specified	3	17%

According to the study by Grönlund and Andersson [2006] the most frequent type of research presented at international conferences is descriptive. Unfortunately, the Albanian research projects were impossible to fully categorize according to research type. However, there were both descriptive research and research projects with the purpose of developing methods and models for e-Service development. There were also large projects where the aim was to first describe and create an understanding of the current situation and then, e.g. develop some e Services or methods for developing e-Services, or there was only a general description of a research program, which embraced several research projects with different directions. However, the division of the directions of the research varies and there is no obvious representation of any direction. According to Grönlund and Andersson [2006] research on e-Services should “focus on the role of ICT in contexts of society, government organisation, method and individuals/citizens, and it should increasingly analyze rather than describe, hence creating and testing theories.”

According to the study there are no current research testing theories in Albania, however, there are a number of research projects developing, e.g. models and methods. The research identified is consequently contrary to the field of e-Government in general, where there is a predominance of descriptive research, according to Grönlund and Andersson [2006].

There are a number of research projects conducted in co-operation between some of the universities. In some cases, there are even instances of international cooperations. Furthermore, there are several research projects conducted in co-operation between universities, research institutes, and other partners, e.g. enterprises, municipalities, county councils, and other organisations. The survey conducted by Grönlund and Andersson [2006] shows a pre-dominance of non-collaboration in the research presented at international conferences. Of the collaboration that actually exists, most are between universities.

In the beginning of the development of the area of e-Government, and also in the development of e-Services, most research was dominated by supply-side factors and there were none or a few efforts that focused on the demand side, i.e. the citizens, businesses, other governmental agencies, and other stakeholders [Löfstedt,

2005; Löfstedt, 2007]. Current interest, however, is increasingly on the demand-side, i.e. citizens. Several researchers point out that a shift in focus towards a citizen and customer-centred service provision is one key to success in e-Government (e.g. [Makolm, 2006; Brown and Schelin, 2006]). However, research concerning user related issues is more frequent today. Interest in the field has started to shift from government at the national level to more citizen-related issues, such as usability and user-willingness. Currently, the “citizen-centric approach” comprises the dominant discourse in e-Government [Accenture, 2002] and the need for greater user participation and involvement in the design and development process has been emphasized in recent years [Ekelin, 2007; EU, 2006b; EU, 2006c; Makolm, 2006; Brown and Schelin, 2005; Ekelin, 2003a]. Albanian research on e-Services also reflects this progress. However, current research projects in Albania have a predominance of governmental focus, but there are nevertheless several research projects that focus on citizens.

Furthermore, until recently the main focus of the research generally in the area of e-Government was on the national level [Löfstedt, 2005]. In current Albanian research on e-Services, research on e-Services at the local government level stands for approximately half as many as the projects on the national government level. There are also projects concerning both national and local levels of government. According to Löfstedt [2007], municipalities express a desire to increase the participation of citizens in order to enrich the development process and the public e-Services developed, and there are a few research projects concerning local governments with a focus on citizens. Several municipalities consider co-operation within their own organisations and with governmental agencies as a strategy to further develop their own organisation.

5. Visions and Trends Concerning E-Services in Albania

Research with an emphasis on the integration of services is being conducted in some of the current research projects as well as research on web portals for different businesses. However, the vision of a “one stop Internet portal” is not fulfilled yet, even though there are efforts striving towards that vision. On the contrary, a trend concerning

integrity has been identified [Tivoli, 2002]. Integrity is present in some of the research projects in progress. Moreover, there are some research projects under way which deal with this issue, e.g., decision support and research on the flow and quality of information.

The Albanian government assumed a strategy in June 2006 for further development of e-Government in Albania. In current Albanian research there are projects concerning methodologies, and methods and principles for the design and development of e-Services.

There are several projects under way concerning organisational change and internal processes. There is also research on co-operation between different municipalities concerning the development and dissemination of e-Services. The digital divide was also discussed as an important area for research and there are projects which are about issues concerning citizens without potential to use e-Services for different reasons. The research projects under way in Albania mostly concern the digital divide in developing countries. The area of e-Services is rather new, and the focus has, according to the study, mostly been on the development of e-Services.

The first concerns the level of computer usage amongst citizens. The question is, according to them, whether or not future users will be more advanced, and thereby more demanding concerning e-Services, or if such development will be hindered. The question concerns, e.g. economic development and the development of the digital divide. According to the study, Albanian research on e-Services includes no research about future demands concerning e-Services from the user's point of view. However, it was found that current research has instead a focus on user-centred e-Service design, i.e. user participation in the design process and usability of e-Services. There was no current research on computer usage and future demands from citizens found in the study. However, some research concerning the digital divide has been conducted, and the focus on user-centred development of e-Services is in line with one of the trends identified by Albinsson et al [2006]. They claim that there must be a stronger citizen/client/user perspective on the development of public e-Services.

The second principal issue raised according to Nordfors et al. [2006] is whether or not we will

see integrated or fragmented governments in the future. This issue concerns to what extent different parts of public administration will work together in the future.

Some of these trends are assessed by them as relevant to the discussion of trends in the further development of public e-Services. According to the present survey study, current Albanian and Kosovo research on e-Services does not include these aspects.

For further research Albinsson et al. [2006] claim that some new areas need to be highlighted and supported in future e-Service development. These areas are: (1) A strong community with IT-support; (2) New types of marketplaces; (3) The citizen perspective as a driving force; and (4) Improved methods and approaches.

There is also increasing interest in the citizen perspective, although there is a need for more research on development where design has users of e-Services as the point of departure. There is also some research under way concerning methods for the development of e-Services in Albania. However, Albinsson et al. [2006] claim that there is a need for the development of improved methods and approaches that secure citizen participation in the design of, and influence on public e-Services.

6. Conclusions

There is currently research being conducted on e-Services at several universities, state university, independent higher education institutions, independent programme providers that are entitled to offer undergraduate programmes, research institutes, and research institutes in Albania. There is also co-operation between several universities and institutes and some of them are also involved in international co-operation in research projects. The research is theoretically as well as practically oriented, e.g. there are research projects on creating the prerequisites for development in the area as well as research projects on the practical development of e-services. The focus of the research projects identified varied and there were different directions at the research. Hence, current research focuses on citizens, communication, the design and development of e-Services, the maintenance of e-Services, e-participation, the quality of services, evaluation, organisational change, interaction between different e-Services,

usability, co-operation, inter-organisational co-operation, accessibility, the development of methods, and process orientation. The present survey study provides a picture of a research area undergoing expansion and change. The reasons for this vary, but one might be the rapid changes in information and communication technology (ICT), and the new application areas and combinations of usage that are being created. This can mean that new and rather unexpected subject areas arise and complement the area. However, this may also cause confusion concerning conceptions, theoretical foundations, and boundaries between and within fields.

Current research corresponds well with international research and also with trends and visions concerning e-Services in Albania. The research strives towards future applications of e-Services, and there are several research projects that create opportunities for the further development of e-Services. Ivanov [2006] says that, "One makes research today on yesterday's visible effects of the use of externally given technology which was adopted the day before yesterday. When the results happen to be published tomorrow they will be obsolete and used to justify new research to start the day after tomorrow about the consequences of today's technology which is already becoming obsolete".

However, the present survey of Albanian research shows that current research in Albania obviously conducts research aimed for the information systems of tomorrow. Grönlund and Andersson [2006] state that a mature research field should include more of theory generating and theory testing, and this is probably the challenge for future research on e-Services.

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THE RELATIONSHIP BETWEEN PROMOTING THE HUMAN FACTORS IN QUALITY MANAGEMENT SYSTEMS AND IMPROVING ORGANIZATIONAL PERFORMANCE OF SMALL AND MEDIUM ENTERPRISES IN ALBANIA

MIMOZA KALIA
FACULTY OF ECONOMICS, UNIVERSITY OF TIRANA, ALBANIA

ILIR ELMAZI
FINANCIAL AND ECONOMIC DIRECTOR OF SIGMA INSURANCE COMPANY, ALBANIA

Abstract

In this study, a sample of 96 Albanian manufacturing small and medium enterprises (SMEs) was studied in relation to human factors (HFs) dependent quality management system (QMS). These were in three distinct industry groups: food & beverage, textiles & garments and leather & footwear. Human factors considered are derived from the seven criteria of the Albanian Quality Award and were used as the basis of a questionnaire survey.

The SWOT analysis for the survey results revealed the urgent need for developing governmental strategies which should focus on improving organizations performance, developing QMS and establishing total quality management (TQM) basic infrastructure for the Albanian manufacturing SMEs.

This paper has provided two proposed practical framework models for improving the performance of the Albanian manufacturing SMEs and for developing their competitiveness in both domestic and international markets, and thus activate their main role in the Albanian economy.

Keywords: SMEs, QMS, Human factors (HFs), Organization performance

1. Introduction

In today's globalized economy system, the Albanian manufactures' sector is facing a deteriorating position in terms of trade, as the Albanian economy faces competitive pressures from international fronts. (Hawash, 2007).

Albanian manufacturing SMEs, as the engine of growth in the economy, have a crucial need to continue to be a

major supplier in the domestic market and to increase their exports and contribute to the Albanian economy (El Mahdi, 2002). However, there are obstacles related to competition and most SMEs are not yet ready to compete for Quality markets. In order to survive in business, Albanian manufacturing SMEs need to strengthen their businesses by upgrading organizational performances and producing high quality products at a low cost. The

acquirement of a new paradigm for upgrading organizational performance and improving product quality is necessary.

Most of Albanian manufacturing SMEs have not implemented QMS because of inadequate understanding of its principles and implementation processes as well as lack of development of organizational infrastructure,

particularly in Human Resource Management. It is time for an appropriate Quality Management approach for Albanian manufacturing SMEs to be introduced in order to solve quality problems. Total quality management (TQM) is considered to be an important management philosophy, which supports the organizations in their efforts to obtain satisfied customers (Hansson, 2003).

Inevitably, the development of Albanian manufacturing SMEs needs to be generated from government support which should assist them to strengthen their business performance immediately and then offer continuous support. Although the government has provided many assistance programs for developing Albanian manufacturing SMEs' organizational performance, these programs seemed to be unproductive. There are several pillars required to be studied for achieving success of SMEs both in the internal and external markets, which have multi-dimensions. The Albanian government, considering the economic importance of the SMEs, should

assist them by formally adopting a productive QMS model for them to follow in order to help them achieving superior performance.

Therefore, in this paper, the identification of critical factors for successful implementation as well as the problems faced by SMEs in implementing quality management system (QMS) are important areas to be understood.

With a better understanding of these issues, it can be a groundwork for the development of an appropriate TQM framework for practical implementation by the SMEs. Moreover, the study results can be used as a guide for the government to develop effective assistance programs for SMEs through a comprehensive vision.

2. Theoretical considerations

Scarcity of academic research into TQM implementation in SMEs has been widely appreciated. According to Temtime (2003), "TQM research has concentrated on large firms. Little has been done on the TQM practices of small-and-medium-sized enterprises (SMEs), particularly in developing countries". Al-Khalifa and Aspinwall (2000), furthermore, assert that "despite the number of publications and the amount of research

into TQM, little empirical work has been carried out in developing countries.

Authors such as Martinez et al. (1998) and Thiagaragan et al. (2001) reported in their studies that there is a lack of empirical studies concerning the critical factors affecting the effectiveness of TQM implementation in Western manufacturing firms. Mersha (1997) indicated, in his extensive review of literature on TQM, that most of the studies reflect the experiences of organizations in industrialized nations and concluded that the implementation of TQM by manufacturing firms in less developed countries (LDCs) is not an easy task, where there are many factors driving or resisting its implementation.

Main purpose of this paper was to increase the understanding of quality management status in SMEs and possibilities of further development towards TQM in SMEs. Since the experiences of TQM implementation in Albania still rather limited, the previous experiences with QMS implementation is used as a departure point. This could be achieved through the following stages:

- Generating knowledge regarding SMEs' work towards improving their organizational performance. This will be accomplished through studying, analyzing and describing QMS implementation processes.
- Demonstrating the industrial organizational performance development needs by means of a case study in manufacturing SMEs (based on the human aspects in the TQM approach) and the need for the government to play a major role in establishing strategies for this development to occur.

This leads to establishing models for, and ways of, implementing supportable strategies for Albanian manufacturing SMEs focusing on the human aspects which should be initiated and supported by the relevant government units.

3. Population and sampling

To select enterprises for this survey, a simple random sampling in which every enterprise had the same chance of being selected was used. Using several data sources was an advantage to the effectiveness of the survey because the choice of enterprises was widened and the possible number

of errors was reduced. A sample of 96 Albanian manufacturing small and medium enterprises (SMEs) was selected in this study.

4. Questionnaire design

The contents of the questionnaire covered the scope of the study, i.e. the human factors in the TQM approach within selected Albanian manufacturing SMEs. The focal point of the questionnaire was the human factors (HFs) section. These questions are generated from the criteria of the Albanian Quality Award (EgyQA). These were:

Strategic human resource planning, Human resource development, Employee empowerment, Performance management, Communication and information management, Leadership, and Continuous improvement.

5. SWOT analysis

Results and observations of this study were analyzed using the Strengths, Weaknesses, Opportunities, and Threats (SWOT) analysis, and a graphical model explaining positive and negative effects on the organizational performance of Albanian manufacturing SMEs were performed.

6. Models developing

The SWOT analysis results were used as a guideline for developing (a) an approach for development stages of QMS (HFs) in the Albanian manufacturing SMEs and (b) a model for developing human resources for establishing an effective QMS (HFs) that assists the Albanian manufacturing SMEs to overcome their internal problems.

7. General enterprises information

Characteristics of the selected enterprises

Market focus

Most of SMEs focused only on domestic market (78.3%) while the rest of surveyed SMEs (21.7%) focused on both markets (domestic and international). No enterprise at all had focused on international market only.

Organizational structure

It was found that 56.3% had an unclear organizational structure chart, while 43.7% did not have any formal organizational structure at all.

Management styles

Only one main management style was used by Albanian manufacturing SMEs. Top down management was the dominant style in the whole sample (100%).

8. The SWOT analysis of Albanian manufacturing SMEs

The survey results (the answers in the studied questionnaire) were analyzed by the SWOT method in order to identify the Albanian manufacturing SMEs' Strengths (S), Weaknesses (W), Opportunities (O), and Threats (T), in order to generate information about their effects on organizational performance and to determine if there is a need to support systems for the organization's development or a need for system improvement. This analysis was used as a guideline for developing the QMS model with focus on human factors.

Albanian manufacturing SMEs have many strengths and weaknesses, and many opportunities and threats which are generated from the business environment and have effects on the whole organization. Strengths of SMEs were confirmed by the results of the questionnaire and should be supported, developed and promoted as a part of the basic infrastructure needed to achieve the criteria of the business excellence practices. Weaknesses indicated the problems and ineffective work systems which need to be solved and improved gradually to get a new and better infrastructure. Opportunities mainly increase the number of international markets open to Albanian manufacturing SMEs. Threats are mainly generated through competitive situations from the international trading competitors and free trade areas (FTAs). There is an increase in the number of overseas competitors most of which have a higher potential for international trade than Albanian firms. Generally, strengths and opportunities influence the organization's performance in positive ways and also support the development of a QMS. In contrast, the weaknesses and threats have negative effects on

the organizational performance, which hamper a successful implementation of a QMS.

9. Strategies for developing quality management system (QMS)

The results of the SWOT analysis were evaluated, and six related strategies for developing a QMS were recommended to be supported by the Albanian government. These strategies should be established and implemented effectively in a wide range for the SMEs.

Strategy 1: Provision of reliable information and effective communication system

Accurate and up-to-date information needs to be communicated from the government to the SMEs, about government assistance programs and international and domestic markets. They should also be made aware of any threats to their competitive situation, marketing position and business performance compared with their competitors.

There is a need to widely promote government assistance programs on offer to support the SMEs to assist in increasing their business performance. Also, SMEs need to have easy access to reliable up-to-date market information, which helps them to clearly understand the market characteristics such as product and customer requirements and the trade law of the trading partners etc.

The government should take responsibility to communicate to SMEs by effectively utilizing different channels of communication such as: newspapers, brochures, booklets, media broadcasting, internet, etc. However, the

information given by these means may still be insufficient to acquire international markets. This gap can be filled by tailoring information seminars and workshops for Albanian manufacturing SMEs to understand market, competitive situation and customer requirements in any particular country.

Strategy 2: Provision of education program

Modernizing its workforce to compete in today's knowledge-based global economy has been a challenge for the Albanian government. With few qualified information technology (IT) skilled teachers and little available content for business and IT education, the level of management and

Information & communication technologies (ICT) skills among Albanian businesses - especially SMEs - is limited.

Recognizing the need to improve education and skills among businesses, Albanian government, in partnership with the World Economic Forum (WEF) and other multinational private and public organizations, launched the Albanian Education Initiative (EEI) in 2005. However, this program needs to encourage cooperation among private organizations and public institutions, as well as supporting effective implementation of its framework to coordinate activities and deliver the desired results.

The lifelong learning and e-learning industry development tracks in particular required a business management and IT curriculum to meet the needs of SMEs through a framework which focus on:

- Enhancing and localizing the business essential course, and creating a comprehensive business management education curriculum for SMEs.

- Developing a nationwide infrastructure to deliver educational content.

An effective implementation of education strategy should prepare Albanian SMEs to participate and thrive in the modern global economy.

Strategy 3: Provision of effective integrated SMEs development programs

The Albanian government emphasizes on its economic policies to develop the manufacturing SMEs in order to increase their competitiveness. These policies need to be effective. Evidence that the current government's policies are unsuccessful in supporting SMEs was concluded from the survey results. Only 30.3% of SMEs had general experience of government assistance. Respondents indicated that they were only interested in very

limited selected topics, not all on offer. SMEs need to be encouraged to trust government. All government programs need to be promoted broadly to all Albanian manufacturing SMEs, even those in small towns and rural areas. The communication channels to achieve this strategy should be selected carefully. The relationship among programs on offer, the requirements of SMEs and the business excellence performance should be

regularly evaluated; and then strategies should be improved to ensure continued development for establishing the best integrated SMEs support program.

This scheme needs to be implemented effectively and there are many ways to do this. Some programs are not difficult to implement e.g. taxation breaks, financial assistance etc. Training courses, consulting, diagnosis of problems etc. should also be available. However, the government may have inadequate staff to support an entire assistance package, therefore, cooperation with specialists from academic institutions, consulting companies, and the professional management industry should be used.

In general, the integrated SMEs support program is an integrated approach for improving the environment and supporting SMEs. It is also a program to implement permanent support structures through which future programs, initiatives and supports can be channelled. The overall objective of the integrated program is to develop and implement an integrated approach linking policy formulation, training and servicing of start-up and existing SMEs assisted by the Government of Albania. The program also aims to reinforce access channels to long term financing of SMEs and start-up businesses.

There are many additional recommendations about actions and activities to be performed on the long run during the SMEs support program included:

- Consultations with stakeholders to (a) identify legislative and regulatory impediments; (b) create new initiatives; and (c) encourage support for program activities.
- Working with legislators and other regulatory stakeholders to propose and implement reforms.
- Developing an overarching SMEs strategy for the next 10 years.
- Launching calls for proposals and assisting in the establishment of a network of business development centers.
- Training and building the capacities of the SMEs support units, and business development services (BDS) providers.
- Supporting the development of the Centers and their services.

- Working with private and public financing agencies to expand financing for SMEs.

Strategy 4: Improvement of organization work systems

The Albanian manufacturing SMEs have to face the threats such as competitive situations, potential competitors, number of competitors, etc. They need an effective organizational performance to respond to real competitive situations.

The weaknesses of the organization performance have caused many problems. About 97% of surveyed SMEs still needed to upgrade their organizational performance to increase their competitiveness. Therefore, all

ineffective work systems need to be improved by government assistance programs.

Generally, this strategy should be implemented and practiced with the tools and techniques designed to improve organization's work systems and to achieve successful QMS, but the research found that most of SMEs had a very limited and poor adoption of those tools and techniques (suggestion system, statistical process control, job rotation) and most of SMEs which applied these improvement tools and techniques claimed that the effectiveness of their application was in a low range. They urgently need to implement an introductory program to widen the use of improvement tools and techniques and to increase their effectiveness by providing advanced training courses for their use.

Strategy 5: Development of quality management system

After establishing a basic infrastructure, SMEs need to develop a QMS to increase their business performance. The basic infrastructures are then set and correspond to the seven criteria of the QA; leadership, strategic planning, customer focus, human resource focus, process management, information and analysis, and business results.

Strategy 6: Establishment of TQM basic infrastructure

The implementation of TQM requires the establishment of an effective basic infrastructure which is considered in the same way as the criteria of the QA which can be used as guidelines for the implementation of TQM and self-assessment for

achieving business excellence performance. In order to establish the work systems in the basic infrastructure, the strengths should be assisted and the weaknesses should be improved.

10. Proposed QMS (HFs) development model for SMEs

The weaknesses in the organizational aspects and basic infrastructures have a clear effect on the implementation and the establishment of a QMS in SMEs. To rectify this, according to this study, enterprises should focus on three development components:

(1) Strengthening the organizational aspects and developing basic infrastructures and organizational culture.

(2) Developing and implementing full QMS; this includes the implementation of continuous improvement (CI), statistical quality control (SQC), quality assurance (QA) programs and best practices.

(3) Increasing the organization's competitiveness by applying full TQM implementation to achieve

world class manufacturing performance or business excellence.

From the above, the scope of proposed QMS (HFs) development approach in Albanian manufacturing SMEs is covered through three stages. These are all affected by opportunities and threats .

11. Developing human resources for establishing an effective QMS in SMEs

From the previous stages of developing QMS in Albanian manufacturing SMEs, it could be concluded that the need of human resources development (HRD) begins with the stage of strengthening the organizational aspects and developing basic infrastructures i.e. strategies, structures, styles and systems. This first stage aims to establish a strong organizational infrastructure and also to introduce a new organizational culture to improve employee performance at each level. Comprehensive management changes are important because they are directly related to human resources (HRs).

To achieve the second and third stages successfully, there is a need to develop HR in all their aspects. This should cover the following:

Managerial education programs for upgrading entrepreneurs to be management professionals (leadership, self-management, decision making, financial analysis, etc.) and how to develop and possess employees' attitudes, beliefs, values, and behaviours effectively, and also how to develop employees' skills.

Delegation and empowerment programs for entrepreneurs to learn how to delegate and empower employees which should be a priority if the owner wants to become a manager of his enterprise. It is the way how to do less to achieve more.

Workplace education and training programs for employees for developing employees' workplace basic skills, technical skills and job-specific training within a broader training framework. These skills are the core skills that employees need in order to do their jobs successfully with high performance. They are also an urgent need to the success of modern businesses.

In this paper, a diagram was developed showing a model of human resources development (HRD) for establishing an effective quality management system (QMS) in Albanian manufacturing SMEs.

12. Conclusions and recommendations

Adoption of quality management (QM) in Albanian manufacturing SMEs was shown to be essential for their survival and growth. This paper focused particularly on developing the organizational performance of the SMEs to make them able to implement a quality management system (QMS) successfully and so they could be able to compete effectively with both domestic and overseas competitors and play a major role for improving the Albanian economy.

The results of the SMEs survey highlighted the lack of human aspects in their approach to QM. It was shown that government assistance, at this point in time, is not effective for establishing strategies for their development.

Most development policies and programs for SMEs which were established and implemented by the Albanian government (GOE) so far were

mostly unproductive and did not clearly distinguish between two objectives; promoting competitiveness and poverty alleviation and income generation.

The government needed to be clearly aware of the needs of Albanian manufacturing SMEs and provide strategies and vision and mission statements to implement its assistance policies in order to develop an effective quality management system (QMS) which would assist the SMEs to achieve a business excellence or world class manufacturing performance.

Alone, Albanian manufacturing SMEs cannot develop their organizational performance. They need to develop linkages with business partners in order to gain business information and assistance programs from as many sources as possible.

The SMEs being supported need to be carefully selected in order to ensure that they are interested in improving their businesses and committed to make the changes that are required.

The proposed strategies for developing a quality management system were recommended to be supported by the Albanian government. These strategies should be established and implemented effectively in a wide range for the SMEs. These strategies were: provision of reliable information and effective communication system; provision of education program; provision of effective SMEs development programs (integrated SME support program); improvement of organization work systems; development of QMS and establishment of TQM basic infrastructure.

Albanian manufacturing SMEs preferred, generally, to use an improved cost strategy to overcome market resistance and refused to use other strategies (product quality, delivery, and flexibility). This was not a sensible response to the establishing of a world class manufacturing strategies which need focusing on all strategies equally. This strategies should achieve three levels of satisfaction; organization, customers, and society.

Quality awards should be created and promoted as tools for awareness of performance excellence and information sharing of successful performance strategies and the benefits derived from using these strategies.

The Albanian Quality Award (QA) should be promoted to be used by SMEs as guidelines

to drive excellence, not to win the award as an ultimate goal. A key to growing both its internal and external markets would be to dramatically improve the quality of how its businesses are run, as well as the overall quality of its goods and services.

The SMEs face a lot of constraints related to its negative structure characteristics. The SMEs' firm size skewed towards smallness and obvious middle firm size is missing, with limited financial resources, and temporarily

hired labour. Skewed pattern towards smallness was reflected in the capitalization patterns of the industrial sector in Albania. They also had an unclear organizational structure chart that was neither accessible nor familiar to all employees, which may limit the long term planning. On the other hand, the SMEs had a long business experience and they are completely owned by families which provide enterprises with flexibility.

Albanian manufacturing SMEs preferred to depend completely on the traditional individual top down management style rather than any other management style such as bottom up or cross functional. They did not use a combined style. Therefore, provision of training courses for developing the management skills of entrepreneurs, managers, and employees about changing the management style from traditional single individual top down to combined (Bottom up, Top down, Cross functional) is necessary.

Most of SMEs in Albania had not established any strategic human resource plan, while some enterprises had strategic human resource plans which were not related to the enterprise's policies and goals. The whole key issues should be given great emphasis; as there are no successful achievements in the strategic human resource planning.

Skills of front-line operators (technical, multi-skills, people, and management) in SMEs needed to be improved.

However, most SMEs did not provide their employees with training courses. The training courses in QM – if provided- were just for once and were only basic courses, which is insufficient for establishing an effective quality management system. The most used excuses for lack of training in QM were motivation weakness of leader, high

cost of training courses, lack of government assistance and less effort from employee.

For human resource development (HRD), it was recommended that;

- (1) Governmental effective campaign to deploy the value of quality award adoption and make it accepted by SMEs owners,
- (2) Enhancement of SMEs' access availability to governmental services and creating comprehensive training support system,
- (3) Frequent provision of training courses for all employees,
- (4) Progression of training courses from basic to intermediate to advanced,
- (5) Communicating to the managers the benefits of the initiative, and
- (6) Encouraging employees involvement, participation and empowerment plans and programs.

Most of SMEs assigned initial authority and responsibility to supervisors for considering and solving quality problems. On the other hand, only top managers could successfully lead the implementation of QM. The work cooperation/teamwork in organizational aspects of SMEs seemed to be very weak, and quality problems were solved by individuals. Therefore, provision of training courses for building a team e.g. team management, team leading, cross functional management etc. is necessary.

The performance management system in most of SMEs had focused only on assisting decisions on work improvement, while there were a weakness and lack in the rest of performance management aspects. The whole subsystems of performance management should be considered, and the system should be developed through three phases:

- (a) Setting expectations for employee performance,
- (b) Maintaining a dialogue between supervisor and employee to keep performance on track, and
- (c) Measuring actual performance relative to the performance expectations.

Policy deployment and document management systems in SMEs need to be further developed to be more sufficient and effective.

Most of SMEs had established many subsystems of leadership and they were moderately implemented. The whole other leadership activities were very weak and some of them were not even found at all in the Albanian manufacturing SMEs, and should be considered and developed to extend to a comprehensive effective leadership system.

In general, organizational aspects should be strengthened before establishing a basic infrastructure. Basic infrastructure needs to be developed through three gradual stages from the foundation of organizational aspects;

Stage 1, Basic organizational aspects (work satisfaction, gender equity and opportunity, employment relation, trust, morale, quality of working conditions) should be established and lead into Stage 2, further development (work commitment/participation, quality awareness, continuous learning, continuous improvement mindset, autonomous work, leadership, work cooperation/teamwork, scientific decision making methods). And Stage 3, which focuses on long term goals and the linkage between employees and organizational goals. From the previous stages of developing QMS in Albanian manufacturing SMEs, it could be concluded that there is an urgent need of human resources development (HRD) in all their aspects.

A small number of SMEs participate in quality award programs. Mainly stated reasons for not participating were that it consumes too much time, distracts from other important matters, and there is no benefit from winning an award. Recommendations for government and organizations about actions to be performed for effectively using quality award programs were as follows:

- (1) Promoting the concept of acquiring quality awards to drive excellence, not to win the award,
- (2) Involving and encouraging leaders,
- (3) Using the organizational language, not the award language,
- (4) Using long term focus,
- (5) Using the feedback from the evaluation process, and

(6) Developing internal expertise.

The SMEs need to implement a simplified version of QMS step-by-step. This would be suitable step to take because it does not consume much time or money and it does not use resources wastefully. Simplified version of QMS is relevant for dealing with poor quality culture of the Albanian manufacturing SMEs.

The SMEs do not have to wait until their organizations are ready to apply for the Albanian quality award (QA). They should use the criteria in the early stages of the journey toward excellence as a source of information on managing, building a common language, and facilitating communication about performance excellence within their organizations. The criteria could be used as a guide for the development of processes focused on performance excellence and for self-assessment and action.

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have to keep in mind that Transparency is not about over-regulating by Bank of Albania or Albanian Parliament. It builds “Fair and Square Communication” between Banks and their Stakeholders developing better achievements for both parts.

2. Stakeholders of the bank

The Bank should define its stakeholders and accurate address information to reveal to each of them. Stakeholders are those individuals or

groups that affect or are affected by the activity of the organization.

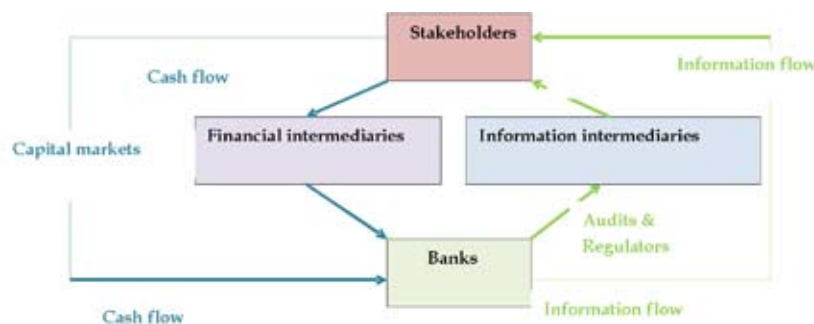
Internal Stakeholders:

1. Shareholders 2. Board of Directors 3. Executive Heads 4. Employees

External stakeholders:

5. Customers 6. Intermediaries 7. Central Government 8. Central Bank 9. Syndicates 10. Competitors 11. Local Government 12. The general public 13. External Auditors 14. Environment 15. etc

Scheme 1 - Relations between the stakeholders and the bank



3. What do we mean by transparency?

Transparency implies openness, communication and accountability. Disclosure (Disclosure) means supplying information voluntarily or in accordance with legal requirements or rules set out in the workplace. Law on commercial companies in Albania, the disclosure refers to providing information on joint-stock companies or their officials, information that can be kept secret if we had to do with a company different from them.

While the disclosure has to do with the explanatory disclosure, transparency as a concept is broader. The disclosure helps transparency. Improvements in disclosure lead to improvements in transparency. Referring to R. Smith, transparency is currently taking a whole new meaning-transparency = active disclosure. This new conception of transparency means not only to let the truth be available, but imposes disclosure or open to all stakeholders.

With the right question: How does the reporting system to improve the governance of banks? The discovery is critical to the efficient functioning of the

banking market causing the transparency to be the best medicine for fraud and market manipulation today. The term “invention or disclosure “ refers to a set of forms of information, such as annual reports, profit and loss account, balance sheet, statement of cash flows and other aspects of this binding or voluntary nature.

4. Transparency and increase the efficiency of banks

Intelligence reporting system and asset information (Transparency) plays an important positive role to improve and increase the effectiveness of bank governance in these areas:

- One of the main functions of transparent reporting system is to limit the discretion of senior management, exp., to “compel” the top management to act not only in the interest of shareholders, or saying in a broader perspective to act interest of the entire bank’s stakeholders (Melis 2002). Protect the interests of consumers of products of the bank; bank’s

shareholders in the long run by reducing the risk of the value of stock and other stakeholders of the bank.

- Discipline of Directors of the Bank. Disclosure and transparency as well as appropriate professional audit, serve as a strong barrier against fraud, corruption, embezzlement and financial scandals, making it possible for banks to compete with what can best offer. So, when behavior-oriented Self-interest tends to shift to financial crime, true transparency sheds light on these various activities causing behavioral changes and strong tendency in the prevention activities.
- A key objective of the transparency of banks is to make responsible the bank leaders (managers and directors). The use of widely accepted principles of accounting serves the need for rich information with a better quality of financial statements and consequently, a higher responsiveness of control agents (Pizza, 2000).
- A transparency of banks depends to a certain extent on the size of information asymmetry that exists between Bank's stakeholders.
- The information "produced" by the system of reporting, satisfy the information needs of bank's stakeholders, also it facilitates the process of monitoring the performance of senior management (and generally control the performance of controller agents) from shareholders who are not engaged directly in the management of the bank.
- The Bank receives some competitive advantage by making it possible simultaneously to increase pressure on other banks for their discovery. It increases confidence in the bank managers, bank and banking market in general by improving the efficiency of investment allocation in banking market.

- Transparency avoids tax evasion and evasion for Provisioning.

In Albania, found that banks consider the issues related to the exposure of information and transparency about mainly as a response to the obligation to respect specific legal requirements governing their business. A part of them argue lack of information publication on not only the requirements of the strengths of not monitoring the implementation of legislation, but also with the high cost (competitors) associated with exposure information.

The information made public through financial statements describes what leaders of the Bank want to become public about the activities and performance of the Bank. And while these leaders are responsible only to some of the stakeholders power (as the biggest shareholders and Board Members), then they continue to have sufficient incentives to reveal only the information that is functional for their specific interests.

Therefore note that in Albania today, must have a true and clear of all the Bank's stakeholders that the banks should take into account the results / consequences of conflicts of interest and the balance of power / strength between the different stakeholders.

The essence of the relationship of the two systems (Reporting and Management) and the balance of power I will present through the scheme 2.

Quality of communication in the corporation reduces the information asymmetry between the stakeholders of the Bank and mostly the interests of deposit customers.

Relationship between reporting system and performance of management / leadership of the Bank is in positive correlation. A good direction affects the quality improvement of reporting systems. Specifically:



- One point of concern in the context of corporate governance is the phenomenon of domination by certain individuals or certain groups. Such a phenomenon probably occurs more often in the model with two levels of management and therefore the management / leadership in Albania is such. As a result, senior management may adversely affect the quality of communication of the bank, making the reporting system to pursue his individual interests rather than objective on presenting true and fair view of the information made public (remember the case of Enron, WorldCom, Vivendi as significant examples of this approach). The presence of a powerful stakeholder / contender, who is prone to unethical behavior, limits the quality of information provided by the bank.
- Transparency improves the process of internal and external audit. External auditors tend to be more associated with management of high level rather than other bank's stakeholders. If bank management system is not functioning properly, the external auditors more closely associated with top management may have incentives to accept the view of insiders (high management) on the development of events rather than to have a view of their own.

5. Transparency Reforms Can Make the Difference.

Yet it is also clear that much more concrete action is needed from Banks, and their stakeholders.

"Top 4" list of transparency-related reforms in a development context (in no particular order):

1. Public disclosure of assets and incomes
2. Effective implementation of conflict of interest
3. Effective implementation (not just adoption) of Freedom of Information to Banks information.
4. Carrying out periodic in-depth Banks diagnostic surveys on Banking Ethics and transparently disclosing to the public the progress and challenges.

While being Lecturer in some different groups of students and civil society I have shared this 'top 4' transparency list during brainstorming sessions. And I asked them to rate their own Bank on each measure. Their ratings have been low on average, pointing to how much more room for progress was needed. Of course it is unrealistic to aim overnight for perfectionism across the full transparency reform spectrum.

The Behavioral Assessment Score for Investors and Banks is another unique scoring methodology that I suggest for ranking Banks based on liquidity, transparency and volatility. Greater transparency and disclosure of bank activities will not prevent banking crises unless appropriate monetary, fiscal, and regulatory policies are also adopted. Nonetheless, greater disclosure of banking problems can reduce the costs of banking crises, even if transparency is not a panacea for preventing banking crises.

"Where sunlight goes the Doctor leaves" an Albanian phrase, it means that is the best disinfectant. These words have become a maxim these days. Sometimes we see some sun rays in some places while the sunshine is totally missing.

In Albania, some NGOs or Public Authorities or Medias even Politicians aired some real stories following a complaint brought up of corruption cases during these last years. Still, they came as result of their conflict of interest not for related to the interest of Society.

Many times Customers, do not have where to call and inform or blame because of deaf public authorities (who should protect them).

The importance of an independent judiciary, alongside high levels of transparency brings as an emergency the role of Albanian Banking Ombudsman still not founded in Albania. Banking Ombudsman is an organization who acts as a trusted intermediary between Banks and their stakeholders while representing not only but mostly the broad scope of constituent interests.

Unfortunately transparency may reduce confidence for those Banks who deserve it. The good news is that transparency can work. When information is relevant, standardized and public, it fosters intelligent decision-making by clients.

Conclusion:

Transparency and disclosure in Albania and in the Balkans, regardless of the progress done, there are still many sharp problems in this field. This situation is partly the product of Cement culture created during the previous centralized system, where reporting were mainly for statistical purposes and for manipulating the reports keeping ahead the orientation of communist leaders.

Public Authorities, Boards and bank key managers as responsible for monitoring the exposure of information are not properly engaged for implementation of the stakeholders' requirements.

Recommendations:

1. Representatives of Public Authorities, responsible for stakeholders protection need to be ethical and professional not just member of Politician Parties.

2. Banks should take care for transparency all the time not only during crises time. Banking is the industry of trust offering untouchable products. (Refer to reforms mentioned above).

3. Transparency, like sunlight, needs to be shining everywhere even where things look to be pretty good.

4. Albanian Government and Bank of Albania should take care for education of Public with concepts banking as a daily lifestyle in programs of High Schools and Part-time courses offers in Training Public Centers.

5. Last but not least, to get the benefits of Transparency must be active disclosure of information as follows:

- Compliance in the use of appropriate accounting policies supported by the judgments and reasonable prudent estimates.
- Maintaining an adequate accounting documentation, as well as an effective system of internal control.
- To be full responsibility of Directors to prepare correct financial statements. They should show fairly the whole financial picture of the bank at the end of each financial year (either gain or loss for that period).
- Disclosure of audit reports. Audit should be responsible for his reporting on financial statements.
- Board of Directors and / or Management of bank should submit a clear comment and exploratory analysis for the main features of its financial statements.
- Detailed reports of the stock option activity based on a clear appearance.
- Evaluation reports of the Board Members, the CEO and the other key managers.
- Full details on the level; shape and total amount of Bonuses of Board Members and Bank's Managers.
- The long term objectives and short term objectives of the Bank.
- The appointment of management and the board members. Their resumes and internal dispersion of the functions. The reasons for their resignations in cases where occur.
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CUSTOMERS LOYALTY AND VALUE KEY DIMENSIONS INTERACTION IN ORGANIZATION

ZHANETA NDREGJONI
MARKETING DEPARTMENT, FACULTY OF ECONOMICS, UNIVERSITY OF TIRANA, ALBANIA

ELSA GEGA
FACULTY OF ECONOMY AND LAW

Abstract

In today world we can talk about mature markets which have different characteristics relative to past and Customers' skill and strength and reduction advertisement effect on him/her are their main characteristics.

Today suppliers in industrial consumption goods market encounter with customers who have unlimited demand, but rarely would be effected with marketing conventional instruments. On the other hand, in the view of customer, market products don't have too much difference with each other in a way that if customer's product commercial brand is not available, he/she will simply replace another "brand" which shows customers' loyalty reduction. Nowadays we can also see great tendency to value in the view of customer between management researchers, and this issue has been analyzed from different aspects. Value concept is one of the most usable ones in social sciences, generally, and in management literature, specially. The important problem is that value in

the view of customer would be determined in the market and with customer realization from what he processes and what he receives, not in the factory and with supplier wants and assumptions. Value is not what would be produced but is what customer gains.

In this paper, we have tried to consider the concept of value and its dimensions, value determiner variable, customer and loyal customer, behavioral approach of loyalty and eventually, customer, loyalty and value key dimensions' interaction in organization.

Key words: value, value key dimensions, loyalty, organization customer.

Introduction:

There is a very interesting concept in marketing literature which is called loyalty and may consist of loyalty to commercial brand, product, services or selling market. Loyalty is: theory and guidance leadership and positive behavior including, repurchase, support and offer to purchase which may control a new potential customer. The concept of loyalty stems into the literature of the customer behavior and focuses on private organizations and jobs.

Marketing surveys are one of the first steps in recognizing buyers and in conclusion are the basis of organizations' management which arranges their job program with considering needs and wants. In past, marketers just thought about hunting new customers and customers' growth had no meaning. Taking every new customer was considered a victory and the existent customers were behaved without any delight and interest. But now, conditions change. Today, with increasing of competition day after day, customer maintenance and growth has become the first goal.

Companies had accepted great cost for taking customers and competitors grab them. These agents have caused goods and service suppliers to promote the quality so that to gain a more share of the market, therefore in addition to attracting more customers and prevent them from scattering they can add new customers to the rest (Kotler,2000).

Recently, considering customer loyalty has increased greatly and today, it would be introduced as an instruction for increasing income. Establishment of loyalty in today's market condition is so hard. Loyalty can be gained but organization should act continuously on this issue and the other thing is that making loyalty in all customers is not possible. A winner relationship should be made between organization and customer. And this relationship would be established in a way that sides feel that there is special benefits for them and attract each other as two poles. Organization should support pure loyal customers with a shield of competitive elements such as price selection, performance development and product promotion.

Value and its dimensions:

Recently, managers and researchers have become more interested in valuable relationships with customers, replacing focuses on exchange and economic benefits. Organizations which reinforce their value giving culture to customers in all processes and activities have more superior commercial performance than others. The concept of value in the view of customer equals to difference between "earned profits" and "paid costs". In this relationship payables and incomes would be affected by recognitions and also customer expectations during seeking activities, earning, using and maintaining of goods or services (Chegini, 2008). Sheth and others in 1991 introduced the theory of consumption value and divided customer value to five key dimensions as:

1. functional value which is related to economic utilitarian and shows the existent advantages in goods and services in the economic view and will point out the functional qualities and characteristics of products.
2. social value which indicates social utilitarian and is an image resulting from having that product in the hands of friends, counterparts and other reference group members in the view of customer.
3. Sensitive value which returns to product sentimental and psychological outcomes, capabilities and abilities of the product in provoking feelings and creation of attractive situations.

4. Recognition value which points out new and amazing aspects of the product and newness and novelty amount of it.
5. Conditional value which is related to a set of conditions which is in front of customer when trying to decide,

Functionality and easy use of Sheth model had caused many researchers to rely on this model. Between these we can point out to a survey done on 2004 in several service organizations of china which has studied customer behavior and his/her value in a complete framework and interesting and profitable results were gained. Scientific and functional investigation of value in the view of customer relating to management performance was the goal of these researchers. Therefore changes happened in Sheth model. Key dimensions of value in their recommended model were functional, social, sensitive and the forth dimension of payable cost or loss. In spite of the existence of two dimensions of recognition and condition, These researchers of Sheth model think that value is not enough complete and functional. Therefore, they have replaced these two dimensions with the forth one and suggested that customers money and unmoney losses in getting goods such as seeking costs, learning, maintenance, financial and social risks and consumed time and energy will be considered in the view of customer, both in longtime and short time (Chegini, 2007).

Value concept in the view of shareholder is introduced as the increase of effect and power of financial markets in financial and accounting texts. Value style in the view of shareholder in selecting company and commercial strategy is based on this attitude that strategies which create the best value in the view of company shareholders would bring the most consistent competitive profit for that organization (Khalifi, 2004). However in final analysis, value increase in the view of shareholder will be done with profitable relationships with customer, not the share trade. Profits and incomes from relationship with customer will influence financial functions of organization considerably, even after time period of connecting with him/her which automatically will increase the share value of organization (Gronroos, 2000).

Value advocates in the view of beneficiaries, consider organizations responsible for value creation of all the beneficiaries, including,

organization personnel and organization and society customers, and in their view sharing in future orientation determination of an organization having benefits in it is their pure right. In value creation studies done for beneficiaries, there is a direct and powerful relationship between profitability and organization growth, customer loyalty, customer satisfaction, given goods and services value to customer, quality of services and also personnel capabilities, abilities, satisfaction and loyalty to organization (Khanh, 2004).

Customer and loyal customer:

Taking more loyal customers will increase company income. For making more loyalty in customers more money should be consumed. Making loyalty in customers in some economic activities have more benefit relative to others. Note that company's investment for making a relationship with customer should be to the amount that the paid costs don't go beyond resulted benefits. In making relationship with customer, there are five different investment levels for company:

1. Basic Marketing: seller would just sell the goods.
2. Reactive Marketing: seller would sell the goods. Additionally he/she will persuade the customer to call him/her, having any question, attitude or protest and criticism.
3. Guarantor marketing: seller would call customer immediately after selling. The goal is to recognize whether bought good was what the customer expected or not?
4. Active Marketing: seller of the company would call customers, sometimes. In these calls they will talk about use cases of the good or new beneficial goods.
5. Communion marketing: company always would cooperate with customer for taking ways of helping him/her for more economy or increasing efficiency.

Developing connections and converting a new customer to a loyal and consistent one, consist of several stages as:

- First Purchase • Repeating Purchase • Special Customer • Attorney • Member • Sharer

Methods

The type of this research is analytical-descriptive. For collecting data, we used field method and questionnaire and in order to analyzing the data, variance analysis (F Test), and SPSS software were used. Statistical society includes all the staff of governmental companies.

Shareholder Company

While customers' consistency and repetition of purchase is very important, companies should make them more depended and interested in themselves with variant ways such as, sending cards, birthday gift, gifts and variant premium (Kotler, 2004).

In developing countries, great effort is done for understanding and measuring customer's loyalty and satisfaction amount and recognition of effective causes. One of these studies was the one with Fornell and his counterparts (1991) in creating a complete and systematic framework for describing agents which are effective in customers' satisfaction and loyalty and on the basis of these surveys, American Customer Satisfaction Index was established. American Customer Satisfaction Index is the first customer satisfaction measurement, which have the ability to describe causal relations between stimulants and outcomes of customer satisfaction. Following public acceptance and recognizing the importance of this index in Europe and America, many countries have determined this index nationally. These indices include, customer satisfaction index in Europe, customer satisfaction index in Switzerland, customer satisfaction index in Malaysia.

1. Customer satisfaction includes product hardware (safety, performance, consistency, elegance) and product conformity with expectations.
2. Understood quality of software (interactional elements in given service) includes, product with services and ease of purchase,
3. Understood image of company, including validity, reputation of commercial brand, and age of commercial brand in industry, advertisement and supplier managers' reputation in company.

Behavioral Approach and Loyalty to Brand:

Behavioral approaches and brand loyalty would measure purchase real behavior of the customer about the product. Purchases propriety method is the most usable version of loyalty to the brand. In this approach all purchase brands of a special good is determined for each customer and the purchases proportion relating to each brand will be determined. Then loyalty to the brand would be measured relative to a kind of arbitrary ratio of purchase relating to the brand. Some of the theorists such as Fournier (1997) or Yao (1997) think that "customer loyalty" would be defined as an attitude.

Describing real behavior of customer on the basis of this attitude is not enough alone, but analyzing and giving a clear explanation of this subject needs considering customer attitudes/ performance structure. But this is true if the concept of loyalty owns real values capable of description and not happening just – wrongly – on the basis of an accident or event. Hard defenders of this attitude are Yakoubi and Chestnut (1978). Others like Guest (1996), Monroe (2005), Guiltinane (2005), Jarvis (2006), Wilcox (2006), Reynolds (2004) and others have introduced ideas in defend of this attitude. Some of the functional indices in the attitude approach include:

- Preference
- Buying Intention
- Supplier Prioritization

Then the approach of attitude from what Jakobi and Chestnut (1978) have introduced, developed to the direction of dependency attitude concept by individuals like Vike (1994) and Baso (Seyed Javadin, 2007). In this concept, two approaches of attitude and behavior were somehow in the same direction. So "loyalty" is shown in a condition that a customer has such a great dependency to a supplier and the purchase cost in the time unit is high. But there isn't such a condition in any of the cases.

Therefore, the main concern of today marketers is to create content and even delight customers with the highest amount of loyalty which needs his/her involvement in the value chain in all organization's processes, actions and decisions.

Results and Discussion

In this base, the hypotheses in this research are:

Basic hypothesis: There is significant difference between various levels of key's dimensions of value, and loyalty and governmental companies customer loyalty.

As the study shows, the amount of sig. is 0.000 and this amount is less than $\alpha=0.05$. So we can conclude that there is a meaningful difference between different levels of key's dimension's of value and customer loyalty.

Hypothesis 1: There is significant difference between versions levels of functional value and governmental companies customer loyalty.

As the our study shows, the amount of sig. is 0.000 and this amount is less than $\alpha=0.05$. So we can conclude that there is a meaningful difference between different levels of functional value and customer loyalty.

Hypothesis 2: There is significant difference between versions levels of social value and governmental companies customer loyalty.

As the table (3) shows, the amount of sig. is 0.000 and this amount is less than $\alpha=0.05$. So we can conclude that there is a meaningful difference between different levels of social value and customer loyalty.

Hypothesis 3: There is significant difference between versions levels of sentimental value and governmental companies customer loyalty.

As the our study shows, the amount of sig. is 0.000 and this amount is less than $\alpha=0.05$. So we can conclude that there is a meaningful difference between different levels of sentimental value and customer loyalty.

Hypothesis 4: There is significant difference between versions levels of costing value and governmental companies customer loyalty.

As the our study shows, the amount of sig. is 0.000 and this amount is less than $\alpha=0.05$. So we can conclude that there is a meaningful difference between different levels of costing value and customer loyalty.

Conclusions and recommendations:

Losing each customer, for every institute doesn't equal to future turn sell, but with losing each one it will harm as much as the purchase of its lifelong and the cost of finding new customer will be added to the last harm. Another negative point is that, it will take several years until the new customer cooperates with the institute as much as the old customer did.

With gathering and studying data from companies which customers repeat buying continuously, Fredrick Reiochheld has concluded that profitability of this group is so higher than others. He says, If a company can increase the customers' repetition of purchase just five percent, its income will increase between 35 to 95 percent (depending on the industry perform in it) (Katler,2000).

About customer's lifelong value we can note that if an institution act with an outflow rate of 20% i.e. 80% suction rate, each of its customers would become a member along a five year period and this means the number of years a that a customer would profit the organization. It can be clearly seen that if the outflow rate decrease to 10 percent (suction rate 90 percent), customer's lifelong will increase from five years to ten years.

Therefore, customer loyalty to production or service values is an issue beyond customer relationship with the institute in an almost long time. A loyal customer is very important, not just because buying more from the company but because he/she will cooperate the company as a moral and material supporter. Interaction between customer and organization with loyalty to the values may happen with a sensitive axis by emphasis on key dimensions of value in the view of customer.

Then, in taking customers satisfaction and loyalty, we should consider function qualities relating to economic utilitarian and the existent profits in goods or services, economically, so that the market maintain and develop with its ever goal.

As it can be shown from the hypotheses test results it can be said that customer loyalty depends on customer consumption value. So, it is suggested producers always consider the level of customers values in production. And this is the most important part in marketing.

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THE IMPORTANCE OF REGULATORY REFORM ON INSPECTION IN ALBANIA AS PART OF THE GENERAL REGULATIONS POLICY

SUZANA GUXHOLLI

Government inspectors are on the front line between the state and the market. Their performance has been introduced recently in developing countries, under increasing scrutiny as the high costs of poor inspection practices for economic performance and the quality of governance in protecting vital public interests have become clearer.

The purpose of government's reform is to set out a series of benchmarks, which can be used as guidelines by reformers. To be able to do it, governments need a ranging from bad practices to good practices to ideal practices, along with suggestions for specific steps that can be taken, referring to positive and negative experiences. There are key findings quite relevant to developing countries.

It has been already proven that, a good inspection system:

- maximizes compliance with clear and legitimate government regulations by detecting and deterring non-compliance consistently and fairly,
- minimizes uncertainty and regulatory risks for businesses by operating transparently and under the rule of law,
- fights corruption by reducing the opportunity for abuse of discretionary powers,
- minimizes costs to businesses and optimizes,

In this article "inspection" is meant as a process that starts once a government regulation has been adopted, - focuses on reducing non-compliance, - and ends with the resolution of any compliance problems.

Inspection refers frequently to inspection visits, but in practice it includes more than it. It encompasses also requests of data by inspectors and filling of forms by businesses (paperwork). As a general rule, inspectorates are organised within administrative units (or even independent public bodies) dedicated to investigations as well not only and inspections. However, the same powers can be granted by the law to officials that are involved in policy definition and implementation. In this case inspectorate refers to enforcement activities carried out by authorised officials. This situation may sometimes raise the issue of conflict of interests but, as far there are no requirements for a functional independence of inspectors, it is compatible with the practice in the EU Member States, especially when human resources to deal with technical fields are scarce and when there is a limited number of regulated firms.

Why a regulatory reform on inspection (the situation before the reform)

The quality of business regulation in Albania is one of the main constraints for economic growth and affects Albania's attractiveness for investors. The existing inspection system is part of the regulatory system and is one of the factors impeding the overall development of the private sector and overall efforts to improve the business climate in the country.

According to the results of the ARC (Administrative and Regulatory Cost Survey, 2005), carried out jointly by FIAS and Ministry of Economy, in 2005 each business was inspected, on average, 13.8 times by 14 different inspections, in other words, the inspectors spent circa 45 days in a particular

business. In 2005 only 4 out of 500 businesses were not inspected (coverage of 99.2%).

Major shortcomings in the existing inspection system, relate to the fragmentation of inspection, poor coordination between inspectorates, lack of detailed provisions on inspection procedures and rules, improper equipment of inspectorates and excessive control over businesses.

Additional findings further to the BERIS survey of June 2008 show that the system of sanctions is not sufficiently deterrent to discourage non-compliance. In addition, was a striking fact that businesses had only a vague knowledge of the technical requirements subjected to the control of inspectors. More significantly this survey showed also an increase of inspections visits between 2007 and 2008. It looked as efforts for a better enforcement but that was also the result of an insufficient targeting of inspections (in relation with the absence of consistent and transparent systems of risk-analysis).

For instance the cumulated number of inspections performed by 7 out of 12 inspectorates which provided data regarding the number of inspections shows 50,000 inspections carried out in 2007 and almost 65,000 in 2008.

To give a rough indication of the magnitude of the problem it was estimated that before the reform, within the scope of inspection reform, businesses in Albania spent somewhat 5,313,429 working days to deal with inspections visits and measurements. The related labour costs amounted to ALL 8,659,349,300 or 86,593,493 USD, in 2008. These figures show that the burden of inspections was significant and was a serious concern for micro and small enterprises, which represented 93% of 107,342 active enterprises by the end of 2008.

Apart of this excessive burden of inspection, other underline shortcomings concerning weak enforcement of legal requirements in almost all sectors of the economy were identified in the Albanian system of inspection. The system was focused on process while modern inspection models shifted already long ago, to a more outcome-oriented system.

Regulatory Reform in Albania and European integration

The reform of the inspection system is explicitly contained in the Long-Term Objectives the Action Plan 2006 on the Regulatory Reform to improve the business climate. The general objective of this horizontal and broad reform is "upgrading the existing legal framework, with the aim to remove the unnecessary administrative barriers and to simplify the whole regulatory framework affecting business". In Albania, in the government's strategy, with regard to inspection, it is specified as an action:

Inspections, with its objectives aim at harmonizing the procedures for inspection along with the methodologies applied during inspections, preserving the specifics according to the sectors needs. The basic methodology is based on the risk analyses approach, but considering any other best international experience of best Review of International Practices, in Inspection Reforms. Inspection, as a radical reform aims also the establishment that makes fully operational the market surveillance structure, which includes all the inspections bodies. The structure already is established to coordinate the reform and to ensure the coordination of ongoing efforts in this area.

The Albanian initiatives for inspections are based on the changing of the mentality from pre-inspection to inspection in the market, assuring all market requirements.

The implementation of measures corresponding to Short-Term Objectives laid down in the strategy and in the annual actions plans (ad-hoc, sectoral measures) has already contributed to improve the inspection system in Albania. In particular, pre-inspections in the context of the issue of licenses and permits have been considerably reduced with the Law No. 10081 of 23 February 2009 on licensing, authorisations and permits in the Republic of Albania. (Licences were reduced as number, from 168 into 42).

The second stage of the regulatory reforms, concerns therefore mostly post-inspections process. That is meant inspections that relate to compliance with the conditions of licensing or compliance with other legal requirements in the course of the activities of enterprises.

Commitments of the Government to advance the programme for European Integration have also resulted in the reform of specific inspections regimes. EU principles on food inspection and framework for inspection, for a number of industrial product-sectors are already set out in the national legal framework (food law and National Food Authority, law on general safety of products and marketing of consumer products) and new organisational structures are currently proposed to the Government to implement these principles (for example, the establishment of a Market Surveillance Agency).

Other initiatives related to consolidation of inspections, include the restructuring of the State Inspectorate for the Environmental and the creation of the State Health inspectorate.

As a whole, the modernisation of inspection has implied efforts to consolidate several inspectorates under the same supervisory authority. (Although that is not required formally by the EU legislation, but that is an approach which has proven its relevance for a better efficiency of inspections in the EU Member States and worldwide).

The Government was and is firmly committed to deliver better results of enforcement programmes, first to provide to citizens the level of safety and welfare expected by them, to allow enterprises to compete on equal footing within the framework of uniform, effective and market-friendly enforcement actions, then, because the enforcement records are closely monitored by the EU to assess the capacity of Albania to cope with the challenges of EU accession.

The reform of Market Surveillance that covers the supervision of a broad range of consumer products (almost all industrial products) can be pivotal to extend similar principles to other sectors of the economy. Principles of risk-analysis, guidance to ensure self-compliance, proportionate and effective sanctions, and knowledgeable inspectors, planning of inspection to target high-risk sectors or businesses are already contained in the Regulation (EC) no 765/2008. This Regulation applies also to all consumer products in the food and the non-food sectors insofar there are no other specific provisions in the EU legislation (principle of *lex specialis*).

Did not fall within the scope of this regulatory the reform of the inspection system:

- Inspection of public services.
- Control concerning direct and indirect taxation and customs. Nevertheless Customs authorities might be involved to exchange information with other inspection bodies in relation with market surveillance of imports of industrial products (market surveillance legislation to be brought in line with Regulation (EC) No 765/2008).

But have not been, left out of inspection activities carried out by local self-governments.

Excessive fragmentation of inspectorates

The Inventory of Inspections in Albania covered 32 inspectorates at the central level. The number of enforcement authorities dealing with businesses is still higher since consider the size of business and of the country. There are out of these inventory, some inspectorates (for example, inspectors of the Albanian Copyright Office, Officials in charge of inspection of ships, Officials in charge of inspections at the Office of the Commissioner for Data Protection, independent regulators such as the Albanian Competition Authority or the Bank of Albania).

Actually the exact number does not matter since each time there are new regulatory areas there are also officials in charge of enforcement of the regulatory requirements. When new institutions were created there was no effort of consolidation (in legal texts concerning procedural rule or with regard to the organizational structures). The issue stands in the fact that the excessive fragmentation has adverse effects. A fragmented system means:

- Inspectorates do not consider the cumulative burden of inspections for businesses.
- They do not either; within their narrow regulatory area have the capacity to evaluate the risks of non-compliance posed by certain economic operators or some sectors.
- In addition, due to frequent and isolated changes in the legislation, there are risks of overlapping investigations that represent costs for the State and unjustified burdens for enterprises.

- Also businesses are more likely to face conflicting opinions from different inspectorates which feeds corruption and on the other hand
- Business need to spend more time to find the necessary information.

Lack of cooperation and coordination among inspectorates

The high burden of inspections was influenced by the lack of cooperation and coordination among inspectorates. Different national and international surveys showed that when inspectors perform joint inspections with other inspectorates and, 7 out of 32 inspectorates said that they collaborate and coordinate their actions with other inspectorates. So no consistent, general and accountable system of co-operation between inspectorates was functioning in Albania.

Insufficient targeting of enforcement programmes

It was obvious:

- the lack of a uniform and clear approach to target inspections,
- hardly inspection programme were based on risk analysis,
- it is not recognised the lack of electronic databases to perform their duties.

In Albania, was a fact that inspectorates did not explain how the priorities are determined without the use of the appropriate tools to do it. Inspections based on views that their annual enforcement programme covered all the firms under their jurisdiction, thing that obviously goes against the idea of risk analysis.

To illustrate how inefficient the system was, it is enough to make the comparison between the number of enterprises inspected by the Labour Inspectorates in Estonia and in Albania (the workforce covered by labour law is comparable). In 2007 the Estonian Labour Inspectorate carried out 4.879 inspection visits while its Albanian counterpart recorded 10.420 inspections.

Vacuum, legal uncertainty and multiplicity in the rules on inspections

It is easy to find out that inspection procedures were unclear and non-transparent. The recent inventory of the inspections before the reform, in Albania confirmed that more than 80 laws (and other implementing regulations) governed inspections, which explains the magnitude of risks of poor legal drafting.

Moreover, it is found out that within the legislative approximation for environmental protection, inspectors create their own rules. So, it was more than necessary, to design an inspection system, clearly separated from the function of regulators. The survey found out, also that enforceable requirements and explanations related to inspections set out in regulations and guidelines, not known by businesses. As a general rule, inspectors gave copy of legal texts at the request of the firms.

The need of a better clarity of enforceable requirements should be part of the portfolio of the regulatory reforms although not covered by the reform of the inspection system. It was included within another component of the regulatory reform (legal database to be accessed by businesses).

By contrast, procedural rules to conduct inspections fell within the scope of the inspection reform because there is no justification to have different rules to govern similar situations. Furthermore detailed rules to implement the most general framework of inspection (market surveillance of consumer products) missing, were considered in the framework of regulatory reforms.

Non-deterrent and ineffective sanctions

The low level of penalties it was not encouraging law enforcement, and the revision of the mechanism to enforce sanctions was needed. (the average monetary penalty, for instance in the area of food safety was ALL 14,400 or approximately 144 USD and ALL 32,391 or 324 USD, in the area of environmental protection).

Although introduced in the Albanian law that implements the EU Directive on the General Safety of Products, it was also clearly evidenced that the concept of proportionate enforcement (best practice to encourage self-compliance), - was not

yet familiar to inspectorates. In the Inventory of the Albanian Inspectorates, where were also exposed the policies of sanctions, the system of warning before imposing fines or other coercive measures was used only by the Fire Inspection Service.

A neglected aspect of enforcement: advice to businesses

In the fast changing technological environment and the frequent adjustments of the regulations to the technical progress, enterprises needs advice from regulators. The inspectorates are at the frontline to provide this advice.

From the review of the websites of a few regulators had shown that 3 major regulators out of 32, provide only the legislation, without other explanatory documents or a Frequent Asked Question section. The majority of regulators did not even provide the legislation.

A survey conducted by the Ministry of Labour show that 34.4% of the respondents request the improvement of data related to legislation. The BERIS survey showed that the advice to businesses did not represent a priority task for inspectorates: in 2008, only 61 and 70 firms submitted formal requests to obtain respectively some guidance from the Labour Inspectorate and the Fire Protection Service. Another fact was that businesses were and still are reluctant to ask questions. There is accordingly a considerable gap to be filled, to meet this objective of priority, such as given to guidance in modern enforcement programmes. This still entail a comprehensive change in the culture of inspectorates and the improvement of the personal communication between inspectors and representatives of inspected enterprises.

Reform undertaken in this sector aimed some general and operational objectives.

General objectives of the regulatory reform of the inspection system refers to the effective implementation of strategies already adopted by the Government to meet the goals of European integration and the implementation of A Modern Regulatory Reform.

In particular the general objectives were:

- To create a modern inspections system in line with the best practice in the European Union.
- To improve therefore health and safety of consumers and workers and to serve other public interests such as health and welfare of animal and the protection of the environment.
- To ensure also competition of economic operators on equal footing as far is concerned the burden of inspection.
- To establish an inspection system compatible with international commitments of Albania and creating the conditions for an exchange of information between inspectorates at the international level.
- To contribute to the elimination of unnecessary administrative burden to businesses so that quality of inspection should be considered as an essential aspect of regulatory quality and performance.
- To contribute to the reduction of the size of the informal economy and to participate in the fight against corruption.

Main operational objectives have been defined in relation to best practice of inspection (in the EU and worldwide). The purpose was to achieve better compliance by economic operators while decreasing the burden of inspection.

In the Albanian context, additional objectives concerned also impacts of the inspection reform on the informal economy and corruption. The Government also addressed these latter objectives by more comprehensive policies given the multi-faceted aspects of the informal economy and corruption. The Government was aware of the fact: a better effectiveness of the inspection system may contribute to the overall success of the Government to implement its policies and successfully fight corruption.

While the inspection reform in progress since a year, it is expected that the operational objectives will be met within a timeframe of 4 years and that performance indicators (outcome-based indicators more than outputs indicators) will allow with transparency, monitoring progress.

The operational objectives aim and consist of the following:

1. To ensure that risk assessment is the foundation of all regulatory enforcement programmes. That is meant the development and implementation of structured and transparent methods of risk analysis supported by ICT solutions to direct inspection resources where they can have the maximum impact on regulatory outcomes and to decrease therefore the burden of inspection for low-risk businesses.
2. To ensure a broad vision of regulatory areas to better target enforcement programmes.
3. That is meant that exchange of information between various inspectorates is expected:
4. To enhance the planning of inspections to allocate resources (including pooling of resources) where they are most needed for a better targeting of high risk sectors or businesses (including the informal economy);
5. To limit the cumulative burden of inspections for businesses.
6. To change the approach to inspections from imposing sanctions to providing advice and preventing violations.
7. To streamline and enhance the fairness of inspections process, in particular to ensure legal certainty and predictability on the scope and due process of inspections (procedural rules including the use of checklists by inspectors).
8. To develop and implement a gradual system of preventive and coercive measures including deterrent and effective sanctions to ensure compliance with legal requirements and to reduce the size of the informal economy.
9. To establish mechanisms of accountability concerning the performance of inspections.

The selection of policy options derives from the study and recommendations provided by international and national experts. Were explored four models currently applied in the region and worldwide. It was created a combined system that is led by a small specific body, called, general inspectorate, that governs all the inspectorates consolidated under 12 umbrellas of different ministries. The general inspectorate deals only with general laws and procedures that regulate

the system, but not with inspections performed by specific inspectorates.

To start the implementation of the reform was established by law the small scale, General Inspectorate and an Uniform, horizontal law on inspection procedures, for all inspections activities, law already ratified by the parliament.

It was obvious that the law will govern only matters not covered by other specific legislation (principle of *lex specialis*). This presumed, that all the Albanian legislation on inspection were subjected to a screening exercise to decide, on a case-by-case basis, what were the provisions to maintain, to amend or to repeal. Streamlining, clarifying and completing procedural rules on inspection concerned the review of circa 145 pieces of legislation on specific inspection regimes (The specific inspection on their side are under the process of consolidation, under 12 Ministerial umbrellas). It is equally important to seek consistency with the Code of Administrative Procedure.

The uniform law has set out the General Principles of the inspection system (vision of the Government on the organisation and methods of inspections).

Worth noting that the two steps, successful reform of the inspection system in Albania, started by the formulation of the EU vision adjusted into local context:

- Inspections visits and measurements to be targeted to sectors that present the highest risk of non-compliance and to be based therefore on transparent and consistent methods of risk analysis.
- Use of resources for advice to enterprises to encourage self-compliance.
- Planning of joint inspections and mutual use of data collected by inspectorates to decrease du
- Plans of consolidation of inspectorates and/ or one-stop-enquiry points for businesses to be negotiated by ministers and proposed to the Government by a given date.
- Development of memoranda of understanding between ministries to share technical expertise, equipment and technical infrastructure.

- Submission of regular monitoring reports to the Government concerning the effective implementation of the principles above in accordance with the template annexed to the uniform law.

Other regulatory and non-regulatory policy options have been taken into account while drafting and implementing the Inspection Reform, such as:

- Training of inspectors and diplomas (professionalization of the function).
- Allocation of financial resources to develop ICT platforms for risk-analysis in a number of regulatory areas and to cover other capital expenditures or operating costs to conduct inspections.
- Sufficient staffing of inspectorates.
- Communication campaigns to raise the awareness of businesses on their rights and obligations in the course of inspection and other communication campaigns on safety requirements.
- Establishment of cost-recovery systems for certain inspections (for example, in the food sector)
- Involvement of the private sector to conduct inspections under the supervision of the State.
- E-inspection as an expert system developed as a generic solution for increasing efficiency and effectiveness of inspection functions. It improves inspector performance, and supports synchronized activities of different government bodies, developed fully in compliance with EU directives and regulations, but also customized to local legal system. It covers all phase of inspection work: Planning; Methodology and document standardization; Risk Management; Registers of: subjects, objects, regulations; Operations; Inspector case preparation; On-field work (including on-line document creation and issuing); Post-inspection work; Document management, digital archive, digital signature; Controlling, escalations, alerts; Analysis and reporting, business activity monitoring (BAM); Internet based

The evaluation of advantages, disadvantages, costs, benefits and risks attached to policy option of the horizontal reform of the inspection system,

was accompanied by careful sector-related analyses, carried out by the national expert and the Government to; evaluate the impact of enforcement of certain sector-related policies.

The examples below give indications on the efforts made by Albania to ensure proper staffing of inspectorates:

Environment

Current situation in Albania: 44 staff

Slovenia: 54 staff

Labour

Current situation in Albania: 144 staff

Slovenia: 87 staff

Estonia: 73 staff

Latvia: 124 staff

Croatia: 154 staff in 2005, of which 27 in the area of labour relations and 77 in the area of health and safety at work. Additional staffing of 53 inspectors in 2008.

Food and feed safety, animal health and plant protection

Estimated staff of the National Food Authority in Albania: 900

Slovenia: 576

Bulgaria: 3262

Slovakia: 2,239

Market Surveillance of consumer products (almost all industrial products)

Albania: Market Surveillance Agency (taking on responsibilities of the Central Technical Inspectorate under the consideration to be outsourced by private sector)) 144 staff of which circa 44 working in the central office.

Hungary: Hungarian Authority for Consumer Protection (2008), 120 staff in the central office, of which 40 work in the central laboratory; 220 staff in its seven regional offices. The authority plans to recruit 150 new staff in 2008.

he three pillars of the regulatory inspection reform were:

- Uniform law on the principles and procedures for inspection.
- Thematic consolidation of inspectorates as far as possible, keeping in mind that consolidation has to be supported by a strategic approach of mega regulatory themes.
- Supervision of the implementation of the reform by a specific body at the centre of the Government (General Inspectorate).

AUDIT AS AN IMPORTANT TOOL OF GOOD GOVERNANCE

SUZANA GUXHOLLI
ADVISOR TO THE PM, PRIME MINISTER'S OFFICE

VJOLLCA KARAPICI
FACULTY OF ECONOMY, TIRANA UNIVERSITY

JUNA DAFA
FACULTY OF ECONOMY, TIRANA UNIVERSITY

Abstract

In recent years, cases of dissatisfaction in reflection and documentation of corporate financial activity, in violation of the objectives and fraud in administration and bankruptcy of banks or corporations, has affected the economy of many countries and have been echoed throughout the financial world.

Starting exactly from these developments and the increased role of auditors in society and demand-offer report for this service, thus take into account the increasing number of companies offering this service to those who require his making, this paper has as the objective to identify the reasons that lead man companies to seek the assistance of internal auditors as well as external auditors to have much more effectively and efficiently in the exercise of their activity and to reduce as many risks as possible which they are faced with.

During the course this paper will discuss about the audit theory and concept, the various risks that may face various entities, the regulation of auditing in our country and in the world, the basic principles that govern the audit of its kind. Following this theoretical approach, to prove the importance of the audit the paper will be followed by a concrete example auditing of the elements of financial statements.

At the end of this topic will be given the relevant conclusions and recommendations arising from the carefully studying of this paper.

Key words: Objectives of audit; internal and external reviews; audit competence; documentation standards; supervision.

1. The need of users for reliable information

The need for detailed review of everyday economic activities, and ensuring transparency in the management of public funds led to the start of the legitimacy of the audit. According to many researchers of audit history, the first traces and testimony about the audit field, were found in the form of commercial laws and accounting reports 8500 years before Christ. With the increasing number and size of entities, grows and become more complicated the governance of such units. As a condition for survival and further development, set out the need for timely and quality information as a basis for governance quality of these units. With the separation of ownership and governance functions (management), is being presented a special group of managers whose owners believe them to manage their capital.

But trying to provide the business efficiently, managers require new instruments of governance. Regarding this, more and more emphasize the importance and usefulness of the audit, particularly of internal audit as a major pillar in the governance of the entities. Since the first development, internal audit has been seen as a kind of external audit compliance. Internal auditors have confirmed the reliability of accounting reports, to reduce the work of external auditors. Exactly this request to users for convenient and reliable information is being created by four environmental conditions:

1. The complexity of events. Events and transactions in today's economy are numerous and often complicated. Decision makers are not prepared to collect and process the information itself. For this reason they need the informing service by professionals.
2. Distance. Decision makers are usually divided by current partners and potential business by physical and time distance, as well as lack of expertise. They need to hire full-time informing professionals to complete those duties that decision makers can't do by themselves.
3. Sensitivity of time. Decision makers in today's highly competitive economy often take moment decisions. They may not have the luxury of expectation some months until they obtain all relevant information.
4. Consequences. Decisions affect the welfare and financial security of individuals and companies. Decisions result in considerable investment of time and money. The consequences are so important as that is an absolute need that the informing professionals obtain reliable and verified information.

Another issue for effective decision making is the presence of risk information (information). Information risk is the risk (chance) that the information (mainly financial,) distributed by a company to be untrue or misleading in a material degree. Decision makers usually get the information they need from companies or organizations that want to do business, to give / borrow or buy / sell stocks. Since the primary source of information is entity itself, there is momentum that the company executives present their business or services better than in reality. This potential conflict of interest is a condition that leads the company to need audit and insurance services. We emphasize that users need more than just information. They need reliable information. For this reason, decision makers employ independent information providers such as auditors in order to reduce information risk. Auditors and other insurance service providers undertake a social role in certification of provided information, primarily the published financial information, offering users of its insurance service that information risk is low. In other words, they serve as an objective intermediary between preparers and users of information and give the information some credibility. This "giving the confidence" can be recognized as security

information. When security is provided for specific certifications made by management (usually for financial information) have to do with providing security in the form of authentication. When the company's financial statements are embedded assertions, then we refer to certification as audit.

Financial reporting function is to provide financial statements for the financial position, performance, change in financial position and disclosure for external decision makers, who have no domestic sources of information such as company directors. Insurance services do not include the production function of financial reporting. Accountants perform this function under the guidance of managers. Auditors gather evidence to assure them to determine if the financial statements information is reliable. The auditors then report users that the information is reliable, expressing an opinion that the company's financial statements are in accordance with accounting standards. This is confirmation of the declaration for the function associated with traditional financial statements.

In conclusion, reliable information helps in making more efficient capital markets and helps people be more clear about the consequences of different economic decisions that are made.

2. Why Audit?

It is adequate to bring attention to some of the numerous examples of bankruptcy of large companies:

- "Enron" (2001) was a multinational trading company with headquarters in Energy Houston, Texas, which fell more quickly when the credit assessment firms prepare their estimates for the company debts. It collapsed because of camouflage and financial manipulation. Enron was the seventh largest company of America at that time. Its leaders hide company debts, which led to bankruptcy and therefore the loss of thousands of jobs.
- In 2002, another huge scandal in the light appeared the scandal of "World-Com's". At first it was a small local agency for the telecommunications, but soon became one of the main suppliers of this industry. As a result of improper actions made with fraudulent spending and capital investment, created an overestimate of the stock market's World-Com.

- In December 2003, Italy made the alarm from a financial crisis that seized the firm's food products "Parmalat". Scandal and the threat of "Parmalat" for the effects of the crisis is called Enron of Europe. The company that produced milk and dairy products during the term deadline, is moribund, after the unexplained loss of 10 billion dollars from its financial accounts.
- In Albania: in 2006 the General Directorate of Internal Audit released the results of the controls exercised in the financial activity of state institutions. Tests and controls that include the period 2003-2005 have revealed alarming numbers of abuses that are committed to public funds. 684 facilities have been audited or 92% of planned audits where 70, 8% were complete audits. Financial damages during governance period 2004-2005 amounts to 1.7 million value of money.

During this period were discovered in total offense with 1,684 million lek economic damage. Economic damages found, compared to the same period last year, have risen 35.9%. While working, the quality and strength of the structures of audit detection is increased. Also violations and damages, which are quite high, coming from the fact that the system of public internal financial control has not worked regularly. 65.5% of claims come from avoidance of customs and fiscal obligations and failure to income tax. Abuses for the year 2004-2005 were ascertained in the Ministry of Transport. In the Ministry of Public Works, Transport and Telecommunications are discovered 70.8 million lek damage, which mainly are Elbasan Water supply sh.a, Albtelekom sh.a in Albanian Post Office and National Housing.

As seen from the examples given above, the need to reduce risks and to benefit from the advantages that today offers a competitive economy, does that decision makers require reliable timely and appropriate information. Decisions to buy or sell goods or services, lend, entering into employment agreements, buy or sell investments and any other decision with economic nature depends largely on the time in which available information is useful. Those who come to satisfy the demand for timely and accurate information are accounting professionals, auditors and insurance service providers. Events such as those described above have led to increased emphasis on corporate

accountability, have led to increased transparency to the way they manage and communicate results to key stakeholders, private businesses and public sector.

Considering all the above cases of various abuses, which have resulted in epidemic consequences for different companies, should highlight why there is a need for certainty in relation to financial and non-financial information. The main reason why we need an insurance service is the fact that ownership and management of a company are not the one who are necessary and are not the same. Insurance services are a key factor to external and internal audit.

3. Audit development in Albania

After 1990 in Albania, the audit mission in the true sense and the relevant standards were not recognized. We find the first steps of this function in form of Control Council, in the government of King Zog and later state inspection and control structures and the system of centralized socialist economy. Like in all countries of East and in Albania, the audit has been represented by economic and financial revision control, organized in nearly all public entities, but this control was directed only on compliance actions and was inefficient and with a high administrative cost. Although essentially all of the economic system was centralized, post-audit control was decentralized, located near the entity but with a visible access to central structures such as the Ministry of Finance to exercise control, in-depth audits throughout the country by creating a mixture of internal audit functions and external one, that influenced by the centralized economy.

Deep transformations in all social and economic life of the country and transforming the economy into a socialist public economy with market rules, dictated the need for improvements and adaptation of control structures in the audit structure and organization of their activities in accordance with the standards internationally advanced, which are based on achieving the objectives of the entity by using public resources with economy, effectiveness and efficiency.

3.1. The main objectives of internal audit

Internal audit is an independent consulting activity that provides objective, security designed to

increase efficiency and improve the functioning of an entity.

In no other country more than in countries in transition, the audit function is important. This is because it has direct impacts on resource management and performance of the general public.

Internal Audit in the public sector is based on several characteristics:

- Under accounting standards, the false statements should be considered material if errors or inaccuracies can influence economic decisions of users, taken on the basis of financial statements.
- One of the main directions of audit work is to assess the internal control system. Internal control is a process of continuous and ongoing activity throughout the participation of all employees of the entity.
- Performance audit has the objective of systematic examination of public entities program, activity, function or management systems and procedures, to provide an assessment of whether the entity in pursuit of goals set and its activity has economic, efficient and effectively.
- For the audit balance sheet, must be considered in all its voices in a row, so that the audit is complete and valid. The same should be said also for the accounts of income and expenditure, as only in this way can become an accurate reconciliation of voices.

The main objectives of internal audit are:

- a) Use the economic, efficient and effective financial and human resources;
- b) Measurement of risk management control;
- c) The extent to which the results of programs audited entity meet its objectives;
- d) Compatibility of activity subject to audit by the legislation in force;
- e) Care for the fulfillment of financial and management data, and their use to support decision making;

- f) Preservation and management of public property assets.

3.2. General principles of operation of the audit

Internal Audit in the public sector based on some principles but the more important are:

1. "Application of the principle of legality", is respect for the Constitution, the Albanian legislation and international agreements which the Republic of Albania is a party.

2. "Application of the principle of independence", is exercise for the determination of the activity, planning, implementation and reporting of audit activity, outside of any influence, which is related to the audited activity or circumstances that may infringe or violate objectivity.

Reputation for objectivity is administered, primarily, by the individual himself in the role of auditors and then by the superior structures.

In order to achieve independence, internal audit structures must:

- a) Be functionally responsible on a permanent basis.
- b) Not have power, executive or managerial powers, authority, functions or duties except those associated with managing the internal audit function.
- c) Not be responsible for detailed development or implementation of new systems, but can give advice before and after such developments.
- d) Not included in the operating control system and operational activities within the public entity.

2.1. Functional independence

Means that audit structures are independent in the planning, execution and reporting of audit results by the entity being audited. Performing the audit done on the basis of rules and standards issued by the Directorate General and the Council of Ministers. Audits are dependent only in respect of work order and rules of ethics and conduct in the civil service.

Internal auditors do not deal only with the organization's financial controls, but with all the organization's internal controls. Help other members of the organization in carrying out their duties and responsibilities, through analysis, evaluation, recommendations and advice. For this reason, internal auditors are considered as internal control of the organization, even its own auditing standards consider the internal audit function as part of the monitoring component of internal control of the organization.

2.2. Organizational independence

Internal auditors independence implies the independence within the organization but not independence from the organization because internal auditors are employees of the organization and therefore do not have the independence of external auditors. In many companies, internal auditors are almost entirely dependent on the company's executive managers. In such cases, internal auditors are only business consultant to executive managers and offering them security objective as well as to executive managers to the board of directors, is limited. Being independent, internal auditors are free to real reporting about the current situation of the organization.

2.3. Political independence

Unlike the functional and organizational independence, political independence inevitably affects not in audit activity, but in the implementation of recommendations and taking actions which it produces from management, where the latter is dependent on the policy.

3. "Application of the principle of impartiality", is objective and transparent documentation of all relevant facts and circumstances relating to the operation of audited entities, without being influenced by personal interests or views of third parties.

4. "Application of the principle of secrecy", is confidential treatment as other data, administered during the audit.

4. External audit and its objectives

Noted that the market is an objective instrument that does not forgive the wrong decisions taken by entities. In fact, every wrong decision, has a "price" that must be paid in the market. Therefore, to avoid wrong decisions to economic units, the governance should be based on real and objective information.

In the context of those information it should be noted, that occupy an important place of accounting information, ie. financial information contained in financial reports. To be real and objective information, so long implicit treatment helps audit issues.

Regarding to this arise the question, which is the real role of external audit in this process? The external audit is a kind of security agreement that an auditor undertakes to provide an independent opinion on a set of financial statements. The objective of an audit of financial statements is to enable auditors to express an opinion whether financial statements are prepared in all the respective material, in accordance with an applicable financial reporting framework.

1. Legitimate audit and non legitimate audit

In most countries, auditors need to be under a national charter for many enterprises, including limited liability companies. While other organizations and entities that follow a lawful audit may include charities, businesses and unions commerce investment.

Legitimate audit could bring several advantages for the company and shareholders. The key benefit to shareholders is an objective trial of auditors. Benefits may include recommendations made in connection with accounting systems and control and the possibility of auditors to ascertain the error and fraud.

Non legitimate Audits are being performed by independent auditors because the company owners, members, tutors, professional or government bodies and other interested parts wish them (non-legal audits), more than the law requires them. Consequently, the audit may be extended to any kind of entrepreneurship that has as product the accounts (some of them may well follow the legal audit), the only merchants and partners. Some of these organizations do not

operate for profit and this has an influence on the nature of their audit.

2. Opinion of legitimate audit

The purpose of an audit, as we mentioned before, is the expression of an opinion by the auditors on the financial statements. Independent auditor's report on a complete set of financial statements requires different elements and format of the auditor's report.

Auditors should consider these elements during the audit:

- Compatibility with legislation: If the accounts are prepared in accordance with the legislation in force.
- authenticity and sincerity of accounts: If the balance sheet is a real picture of the company's figures at the end of the period and income statement (and its CashFlow) present a true picture of the results for the period.
- proper records: If you are required to keep records of accounts for audit.
- Compliance with records of accounts: If the accounts are in accordance with the relevant records.
- Consistency of other information: If other information attached accounts are consistent with the accounts.

3. Advantages of non legitimate audit

Audit of accounts of a partnership, for example, have seen these advantages:

- Can provide a wealth being divided between the partners accounts.
- Where audited accounts are available, this may make them more acceptable to the tax authorities.
- Sale of business or the negotiation of the borrowings and overdraft facilities, can be facilitated if the firm is able "to produce" audited accounts.
- An audit on behalf of a "non-active partner" is useful since the moment when such a person perceives different business checking accounts

or confirm the division of benefits due to him or her.

4.1. Internal audit versus external audit.

There are differences between internal and external audit. The main differences between them are:

- Internal audit focuses on the organization's operations, while external audit has to do with giving an opinion on the accuracy of financial statements.
- Internal auditors often are employed in the company, while those external are independent of the company and its management.
- Internal audit reports are for private management, while external audit are available for all.

Summarizing differences between them:

1. Objective: The internal audit is an activity designed to add value and improve an organization's operations. External Audit enables auditors to express an opinion on financial statements.

2. Report: Internal Audit reports to the board of directors or others, charged with governance as the Audit Committee. These reports are for private management. The external auditors report to shareholders or members of the company on the accuracy of accounts. The report is publicly useful.

3. Field of activity: The internal auditor's work is related to the organization's operations.

The work of external auditors is related to financial statements.

4. Relations with the company: internal auditors are often employed in the company, although in some cases function as external sources.

External auditors are independent from the company and its management. They are appointed by shareholders.

Conclusions

From studying this paper, we arrive at some conclusions. However is to be mention the fact that the auditing field in our country, is still in its

first steps in terms of its genuine development. Thus, for a better performance of this field we give some recommendations that can be considered to be important.

- Given that our country follow different models of financial reporting, often legal framework of financial reporting for economic units is not harmonized. Financial reporting requirements for commercial companies, are important because of current and potential impact on banking intermediation, tax collection and tax transparency and financial discipline. Limited financial intermediation is growing rapidly and most of the portfolio of loans given is in foreign currency. Important position of foreign exchange rates and rapid credit expansion requires a more rigorous financial reporting framework which will assist in registration and evaluation of assets and liabilities of banks and will control the exposure of banks and borrowers from the exchange currency risk.
- There is a need for stronger application of rigorous reporting for legal auditors transparency of public interest entities in Albania. Transparency reporting by these law auditors will facilitate monitoring and supervision and will further strengthen public confidence in the statutory audits of public interest entities and sustainable development in these sectors.
- The need of drafting a law for the audit, to establish and make operational a system of public oversight of auditing profession, a high control quality of statutory audits and regulations on registration of domestic and foreign auditors, including auditing firms, is considered very important.
- Quality Control for the statutory audit is very important to ensure a good quality audit, which increases the reliability of published financial information and gives value and protection to the shareholders, investors, creditors and other interested parties.
- Recommended the establishment of an effective system of investigations and sanctions to detect, correct and prevent inadequate performance of the statutory audit. Any measure or sanction is imposed on audit auditors or legal entities, should be made known to the public.

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IIA Standards

ANALYSIS ON THE RECENT AMENDMENTS OF THE ALBANIAN LAW “ON COMPETITION PROTECTION” IN ALBANIA

ERIONA KATRO
KESTRIN KATRO

Introduction

Crisis and the disappearance of the socialist regime in Albania brought the need to transition, for the construction of pluralistic political systems and the need for economic and political innovations. Albania lived a difficult transition, which was initially directed toward Western models. Regarding the economic transition, the first law “on the main constitutional provisions” set on the basis of the economy “and ensuring recognition of diversity of property and free economic initiative.”¹ This constitutional provision has a fundamental historic importance, because it marks the passing of this small country from a centralized economy system in the market economy system. It is precisely this moment when begins the creation of the Albanian market and the protection of that which would be called competition right in Albania.

At the same time with this initial step of economic transition started the economic and diplomatic relations between the European Community and Albania.

The first norm on competition protection in Albania is the law no. 8044 of 1995 which was entirely an innovation for the Albanian system of law. First for the anti-competitive behavior that worth to attract the attention of the legislator in this law is the dominant position which is penalized regardless of whether or not brings market distorting effects. It is clear that this discipline havoc on a target anti monopolist complex, based on the objectives of economic policy in favor of small and medium industry conceived as the only able to produce positive effects on the developing market. Even the way of regulation or restrictive agreements distorting competition appeared completely rigid and regulated differently from the European Union, since it does not allow exceptions to the

ban. These predictions find solid justification in the delicate economic situation in which the country stands. The first discipline that acknowledged competition for social and economic necessity was “the need to create a market.” Based on this need we can state that the first function of law was the protection market as a form of market development and the economy in general. Albanian legislator was audible, that once market mechanisms and market stabilization functioning as a market should function in a market economy system, then it would intervene again with a new legal regulation in line with European discipline. And so it happened. The law remained in force until 2003 with the approval of law no. 9121, 28.07.2003 “On Competition Protection.”

At the same time the EU relations with Albania were involved to bring the signing of an association agreement which was signed in June of 2006 by entering into force on 1 April 2009. This paper will briefly analyze the recent changes in the 9121 law “On Competition Protection”, in relation to provisions that discipline prohibited behavior, meanwhile highlighting the impact of EU on the creation and evolution of this discipline.

Current norms on competition protection.

With the approval of the Law No. 9121 “On Competition Protection” it was passed from an economic normative function in a new normative that protects competition in the market conceived as a form of improving the welfare of consumers and a better distribution of resources. It was a move that aimed to achieve that at the time of adoption to see the competition and the result entirely in line with market evolution process in Albania and the process of legislative approximation of European market discipline.

Law no. 9121 "On Competition Protection" was drafted with the main idea of fulfilling the duties of a country into entering in the European Union. At the time in which had begun the drafting of the project-law negotiations for the drafting of the Stabilization and Association Agreement with Albania on one hand and the European Union and Member States and on the other hand. Through this agreement Albania commitment was to progressively align its legislation with the Community, to contribute on establishing a free market space by carrying out necessary reforms to achieve European standards. In this agreement the parties agreed to strengthen the economic freedoms that are based on the agreement and apply free market principles, the obligations that the Albanian legislator decided to conduct in the competition field with the approval of Law no. 9121, 28.07.2003 "On Competition Protection."

Law no. 9121 "On competition protection" has seven parts. Innovations brought about by this law compared to the previous law affecting the discipline of prohibited agreements, abuse of dominant position, concentration and for the first time provides the establishment of an independent structure who is entrusted for normative implementation.

The first part is entitled "General Provisions", it defines the function of the law, its scope and in this first part are given some of the most important terms of competition disciplines.

The second part defines prohibited agreements, abuse of dominant position and concentrations.

The third part of the law entitled "The competition authority and administrative procedures" establishes the first independent administrative structure, guaranteeing the implementation of the normative. In determining the rules of the creation, organization and functioning of this structure, the legislator is uniform with the law "On Competition Protection" of some European Union member states. It should be clear for all of us that a competitive market requires the rules of competition to be safe and applied with technique, according to the objective criteria.

It is precisely for this reason that the pattern of European Union member countries Competition Authority is always imagined as an administrative institution, independent and characterized by technical competence of a very high level. On

the EU integration the existence of independent authorities guarantees for competition emerges as vital to European institutions as creating uniform systems and joint management, technical and safe, facilitating the process of approximation of legal systems and administrative integration. The Competition Authority is composed of two structures: the Competition Commission with the decision-making power and Secretariat which has an administrative function. Authority carries out its activity with the mission to use of legitimate means to protect and promote free and effective competition for a functional market and with an ultimate goal that is the realization of the greatest benefits for consumers.

Regarding administrative procedures, law defines the general rule under which "will be applied the provisions of the Code of administrative procedures only in cases where the law no. 9121 do not determines the contrary , "and determines the subsequent sections, in line with EC Regulation 1 / 2003 antitrust defense system.

The fourth, the fifth, the sixth and seventh arrange governing civil procedures, the cooperation of the Authority with other institutions, administrative violations and penalties that are being applied and closes with the last transitional provisions.

The law deals only with economic competition, leaving unfair competition to the competency of Albanian Civil Code. Unlike its predecessor, this law applies to any public or private entity which is part of a commercial activity.

In the frame of obligations fulfillment taken by the Albanian State association and stabilization agreement, the Council of Ministers determined two types of priorities to Albanian Competition Authority: short and medium term priorities. Short term priorities consist in the perfection of Albanian legislation and the enhancement of institutional capacities of the Authority. Medium-term priorities consist in effective implementation of the law "On competition protection". The implementation of these priorities become a necessary simplification of the law "On competition protection" to make it more simple conform the specifications of the internal legislation and in order to approximate it thoroughly as European competition legislation. This necessity became a draft-law which was voted in Parliament in September 16th, 2010.

Changes made in the law “on competition protection” affecting the entire discipline are mainly changes in formal terms - resettlement of linguistic provisions and also some essential changes.

Prohibited Agreements

The second part of the law deals with the prohibited agreements. The legislator has dedicated four articles to the agreements, from Article 4 to Article 7 of Law no. 9121. Specifically Article 4 in line with Article 101, paragraph 1 of the Treaty on the functioning of the EU prohibit all agreements which are prohibited for the object or effect (Prevent, Restrict or distort) inhibit, to tighten or distort competition in market. The law applies to any agreement: formal or informal, explicit, horizontal or vertical. After determining the general prohibition of Article 4 explicitly defines certain activities in which will be concrete the prohibited agreements by recalling the text of Article 101, paragraph 1 TFBE's: Aligning of these activities does not have exhaustive value. The second paragraph contains provisions of civil sanction and invalidity of agreements prohibited under Article 4, paragraph 1.

Even in the Albanian system is in effect the general rule according to which agreements that restrict competition should be prohibited because from a static aspect they reduce overall economic welfare (and in particular that of consumer) and a dynamic aspect, can eliminate the incentive that causes competitive pressure on innovation and technological progress.

Before the amendments approved by Law no. 10 317, 16.09.2010 “On Some Additions and Amendments to Law no. 9121, 28. 07. 2003 “On Competition Protection,” Changed “Albanian legislator attempted to summarize in three provisions what is foreseen by the European legislator in the exemption regulations, in a large number of provisions, in order to make it clearer for operators of the market when the agreement accomplishes the conditions of exemption. Thus, Article 5, in line with Article 6. 101, third paragraph of TFBE and in line with the Commission communication no. 2001/C3/02 on horizontal agreements, Articles 24, 31 and 32 and Regulation n. 2790/1999 on the application of the third paragraph of Article 81 of the ECT to vertical agreements and concerted practices, Article 4 / b contains the discipline of

exceptions from the prohibition of horizontal and vertical agreements. While Article 7 contains the exemption agreements of the license. Article 5 defines the conditions in the presence of which is possible that the individual exemption from the prohibited agreements under Section 4 (in line with Article 101, paragraph 3) in all those cases where the agreement in its complexity brings several benefits, as the economic welfare, which compensate the competition restrictions. While Article 6 recognizes the right of the Authority to adopt regulations of the exemption implementing from Article 4, paragraph 1, for certain categories of agreements. Article 7 establishes the possibility of exclusion from the prohibition of agreements (of little importance) *de minimis*.

Abuse of dominant position

Albanian legislator has left to the abuse of dominant position two specific provisions such as Sections 8 and 9 which are modeled after Article 102 TFBE's. One of the most important innovations of the new law is not punishment of a dominant position, but the abuse with this position are not defined exhaustively in some situations, which may constitute abuse of dominant position. This kind of discipline is not only a definitive break from the discipline of previous legislation, Law no. 8044 of 1995 in which the prohibition of dominant position such as justified by the conditions of the Albanian economy, but an approximation to the discipline and community. Before recent changes of the dominant position defined as “the position of one or more enterprises, allowing them to be capable, in terms of supply and demand, independently of the other participants in the market as competitors, clients and customers”.

As noted this definition only concentrates on the skills of a design undertaking own trading strategies without any condition suffered by the other actors in the market. This provision lacked any reference to “the ability to prevent competition” referred to the Community definition given by the Court of Justice. The provision is not referred to the economic situation resulting incomplete. These were the reasons that led to modification of the provision by approximating it with the community definition.

Albanian legislator establishes in Article 8 the criteria for the assessment of dominant position

which have remained in their original version as they are correct and in line with Community requirements. At the community level these criteria derive from a consolidated practice of European Commission and the Community jurisprudence.

The content of Article no. 9 has been the subject of Legislative review of which defines the cases that may constitute abuse of dominant position. Original version provisions consisted of 3 paragraphs. In the first paragraph sanctioned abuse of dominant position: "Any abuse by one or more undertakings of a dominant position in the market" It was an ambiguous formula as the result left to think that it is prohibited any kind of abuse by an undertaking in dominant position, namely the abuse of nature different from those of dominant position. But on the other hand the purpose of this provision is the prohibition of abusive exploitation of a dominant position. In fact, after intervention of the law the above definition results processed in order not to leave space for assumptions "it is prohibited any abuse of dominant position by one or more undertakings, which hold that position in the market."

Modifications have affected the 7 categories and definitions of behaviors that constitute abuse of dominant position. Legislator has intervened to make a disposition of formal provision mainly by summarizing the 7th projections of the above behaviors within the 4 categories contained in Article 102 of TFBE -se.

In the third paragraph, which is now repealed, a possibility envisaged exemption from the prohibition "shall not be considered abusive practices of one or more undertakings of a dominant position in the market if these companies prove that they committed to objective reasons, such as technical or legitimate trade reasons. " This was an ambiguous provision as it was not specified what should be implied by "technical reasons or because of legitimate business" or what the parameter on the basis of that which had authority to conduct its assessment by recognizing in this way to emphasize a discretion of the Authority.

Concentrations

Discipline of concentrations is provided in Articles 10 to 17 of Law no. 9121. For the preparation of these articles in their original version which is mainly consulted to the old rules on concentrations

Community (EC) n. 4064/89. Among other resources that have served as important model, it is known the position of the Regulation (EC) n. 1 / 2003 on the application of competition rules under Articles 81 and 82 of the Treaty. And this discipline has been changed by recent modifications made by Law no. 10 317, 16.09.2010 "On Some Additions and Amendments to Law no. 9121, 28. 07. 2003 "On Competition Protection."

In the original text of article no. 10 of the law 9121 legislator determined that "we have a concentration when carrying out the cases determined in the clause" by not referring in any moment "sustainable change of control" which in reality constitutes a key element in the definition of concentration. In an economy respective, a concentration is achieved every time that a) there are at least two enterprises with autonomous decision making, b) where after the concentration we will not have some decision-making center, but a common center, c) final result of this process is the modification of ownership or executive structure of at least one of the undertakings. On the legal frame, concentration represents the outcome of a process which can be achieved through a variety of alternative instruments that are between them in terms of form, but are equivalent in terms of substance, as are all able to produce lasting change time structure of the undertakings concerned. It should be noted that errors or omissions by the legislator has changed the definition of concentration and present results of complete and accurate and is not limited to forecast a series of legal actions through which the concentration operation can be realized, but in a way identical set in the Article 3 of the Community Regulation no. 139/2004, that: "Concentration of undertakings is present in cases where a change sustainable occurs, because of"

Albanian legislator lists the three legal actions through which a concentration may be realized and that are almost identical to the actions indicated in Article 3, paragraph 1, points a and b. the Community Regulation no. 139/2004. . But the provision in the original version determined (not now) and creates a common undertaking of concentration as a possibility ... "when a joint venture, that performs all the functions of an independent entity." This provision seemed to be referring to full function joint establishments without specifying whether joint enterprises should qualify as a concentration in the presence of coordination

risks. This weakness is regulated and determined in the provision closing the "Creation of a joint venture does not constitute a concentration under this section, if there is any object or activity due to competitive coordination between two or more independent enterprises. In this case, the creation of a joint venture is estimated on the basis of Article 4 of this law as an agreement"

" So we notice that the legislator is unified with the solution to this problem given by the previous regulation of concentration, reg. 4064/89.

In the original text of Article 13 prohibiting concentrations which is expected to create or strengthen a dominant position to one or more undertakings inspired by Communitarian old Regulation no. 4064/89. This wording is now changed by uniformed current concentrations with actual Regulation of concentration no. 139/2004: "The Commission prohibits concentrations of the undertakings, limiting significantly competition in the market or a part thereof, in particular, as a result of the creation or strengthening of dominant position". New Criterion integrates with the objective dominant position "to evaluate the effects that may have concentrations in the oligopolistic markets."

Even Reg. 139/2004 sets out considerations that in the oligopolistic markets, in particular situations, concentrations that lead to the elimination of competition between undertakings participating in concentration as such: Reduction of competitive pressure on other competitors, is possible even in the absence of coordination between members of oligopoly, to create significant barriers to effective competition in the market. "

As it was said is an aspect which was not previously taken into account not from the Regulation.4064/89, neither from jurisprudenza, community nor from Albanian Competition Authority. In the interest of safety of law provision was modified by integrating criteria of dominant position by the criterion of "substantially restricting competition" in the law no. 9121 to 2003 ".

Another change in this provision is related to a categorical ban done to the Commission and latter on it might try to undermine concentrations in cases where its registered office seriously jeopardize the bankrupt when there was no other option less anticompetitive than the concentration to save enterprises for undertaking bankruptcy. This provision was justified by the fact that one of such enterprises is destined to emerge from the market

and its failure would bring as a consequence the creation or strengthening of a dominant position of the market as the place of one undertaking would be occupied from another undertaking. Therefore it is considered that competition is harmed more from the failure of undertakings than from the authorization of the concentration of undertakings.

This kind of definition is left in the law, but is tamed because it is thought that more space must be left to decide the Authority to consider whether or not a situation of enterprises in difficulty by evaluating all elements of the concrete case. Especially important is the increase in the provision of "Efficiency Defense" in trials evaluating the concentrations even this forecast is based on community of the precise disciplined lines of the European Commission guidelines, for assessment of concentrations where in the title VII is treated the growth of efficiency due to concentration.

The Commission clearly recognizes (paragraph 76) that the actions of concentrations may respond to the needs of a dynamic competition and be able to increase the competitiveness of industry " , bringing both in terms Advantages manufacturing efficiency, both in terms of dynamic efficiency" Also among the modifications other disciplines can not mention the extension of deadlines for notifying the Authority (from 7 days in this period exceeds 30 days) or changes the definition of turnover of the participating undertakings, the concentration needs to be notified through which is expected to concentrations increase in reports of the Authority. I think this is a modification of the specifications right on the Albanian market that the market is a small country where a series of small, medium and some large undertakings operate mainly.

Conclusion

Recent changes in competition field through Law no. 10 317, 16.09.2010 "On Some Additions and Amendments to Law no. 9121, 28. 07. 2003 "On Protection of Competition" has entered into force nine month before. These changes that have made possible the simplification of the law to make it more understandable, to conform with the specifications of internal and aligned in order for them to complete with European competition legislation and legislation of some Member States enabling thus ensuring the same standards of protection offered in other regional countries which

are candidates for EU membership or the member countries. In this work it is highlighted the fact of how strong is the impact of European Union rules on production in the competition field. The evolution of these rules has a primary purpose which is to develop the internal market and its integration in the European market.

Endnotes

1. Economic and political reforms initiated around 1992. Particular importance was paid to the process of privatization, liberalization and stabilization of price and trade, development of foreign investment, reforms in banking and financial statements.
2. The first diplomatic relations and economic ties with EU date back in 1991-1992. The first agreement on exchanges and trade and economic cooperation was followed in time by many other deals, the result of perseverance, the desire of the Albanian government to stabilize and consolidate democracy and to promote economic and social progress the prospect of opening negotiations on a Stabilization which will subsequently lead to the Europeanization of our country's official. European Community newspaper, L 343, 25.11.1992 pp. 0002-0009.
3. We have to consider the bill drafted in 1994, only three years after the former totalitarian regime, from a totally centralized economy where there was no concept of the term "private property and economic freedom." Formally the free market had begun to emerge three years ago, but in reality Albanian Market in those years was a real mess. The problem of market concentration was dominant, as in a small market in terms of a limited offer can only operate a few operators and discourse of an operator in a dominant position will serve as a distorting the market mechanism. Legislator at the time was fully aware of the situation.
4. It had no time left for all actors in the market to understand to what initiatives consisted of economic freedom and freedom of the undertaking and what was a free market and should be understood as rules of conduct in such a market. Moving from a system where there was a market in a newly created system where the market may not be accompanied by classical competition rules that assume a higher sense of accountability and honesty from the actors in the market and a culture on competitiveness.
5. Pursuant to the obligations laid down in Article 84 of the Competition Authority law, since the beginning of its operation, approved the regulation "on the organization and functioning of the Competition Authority decision no. 2, of 17,03,2004, n.1 published in the Official Bulletin, 2004-2007, Tirane 2007, Regulation on the implementation of procedures relating to concentration between undertakings "is based on the old regulation EC 4064/89 community concentrations, regulation "on fines and reduction of the value, "which was designed to support the Commission's 2003/C communication. EC 10/13 "Communication on immunity against fines and reduction of value of fines in case of agreements between undertakings --- Decision No. 9, 01.06.2004 published in Official Gazette n. 1, 2004-2007, Tirane 2007. On approximation of European acts such acts be seen the decision of Council of Ministers n. 463, dated 05.07.2006. "On approval of the national plan for implementing the Stabilisation and Association Agreement", section 3.6/2.2. Official: 2006, n. 80. pg. 2307 and the adoption of procedural rules on spending before the Authority, Decision No. 10 of 29.06.2004, published in the Official Bulletin No. 1, 2004-2007, Tirana, 2007 At the time of writing, the Authority is working to change the rules on penalties in order to make it more compatible with Communication 2003 / C 10/13 EC "Notice on immunity from fines and reduction of fines in cases of agreements between undertakings", Decision No. 9, and with Regulation (EC) No 1 / 2003 of December 16, 2002 for the implementation of competition rules under Articles 81 and 82 of the Treaty, Official Journal of EC, L, 4.01.2003
6. Pursuant to the obligations laid down in Article 84 of the Competition Authority law, since the beginning of its operation, approved the regulation "on the organization and functioning of the Competition Authority decision no. 2, of 17,03,2004, n.1 published in the Official Bulletin, 2004-2007, Tirane 2007, Regulation on the implementation of procedures relating to concentration between undertakings "is based on the old regulation EC 4064/89 community concentrations, regulation "on

- finances and reduction of the value, "which was designed to support the Commission's 2003/C communication. EC 10/13 "Communication on immunity against fines and reduction of value of fines in case of agreements between undertakings --- Decision No. 9, 01.06.2004 published in Official Gazette n. 1, 2004-2007, Tirane 2007. On approximation of European acts such acts be seen the decision of Council of Ministers n. 463, 05.07.2006. "On approval of the national plan of implementing the Stabilisation and Association Agreement", section 3.6/2.2. Official: 2006, n. 80. pg. 2307 and the adoption of procedural rules on spending before the Authority, Decision No. 10 of 29.06.2004, published in the Official Bulletin No. 1, 2004-2007, Tirana, 2007 At the time of writing, the Authority is working to change the rules on penalties in order to make it more compatible with Communication 2003 / C 10/13 EC "Notice on immunity from fines and reduction of fines in cases of agreements between undertakings", Decision No. 9, and with Regulation (EC) No 1 / 2003 of December 16, 2002 for the implementation of competition rules under Articles 81 and 82 of the Treaty, Official Journal of EC, L, 4.01.2003
7. Market regulation made by the Law no. 8044 .The year 1995 (first law) fully depreciated by up to privatized leaving the possibility of activation of the investigation procedure at the Competition Directorate. It is worth to highlight that the Competition Directorate had no power needed to undertake an investigation on its own initiative and as well to understand this huge gap in the law translated into silence and perhaps could even call "vegetating" the this authority. Evidence is the fact that until 2000 there is no decision of the Directorate. A weak point of this discipline, even this countercurrent with what happened in the European space, was the placing of the Competition Directorate under the Ministry of Economy. While the law no. 9121 of 2003 (current law) has increased the Authority more powers in his public function as guarantor of the implementation of the law on protection of competition. In fact, one of the novelties of this law, in comparison with the previous one, except the independent character of the Authority, is recognizing the competence of the Authority to launch an investigation mainly (ex officio)
 8. Reference model for competition law are taken from: the law Belgian, French, Italian, German, Danish, Norwegian, Finnish, Dutch, Croatian, and Slovenian.
 9. With the decision n. 463 dated 05.07.2006 "On approval of the national implementation plan of stabilization and association agreement", www.qpz.gov.al
 10. The Competition Authority stated that during the implementation of the law is found in front of a number of problems as in violation of provisions, weak collaboration between institutions and entities that should apply the law, the need for improvements and amendments to provisions on procedures and sanctions applicable, problems those arising as a result of difficulty in understanding the provisions of law not only by the operators in the market, but by different institutions. Report on the draft law "On some amendments to Law 9121, dated 28.03.2003" On protection of competition "." Albanian Competition Authority source.
 11. Through these modifications required to achieve: 1) realization of a better protection of the market and a law enforcement under the Acquis Communautaire seeking to achieve the same standard of protection to other countries in the region which already enjoy the status of candidate country for membership EU, 2) perfection of the advocacy function and increase awareness to consumers on the right or indirect benefits derived from the concept of competition as "a right and public good at the same time", 3) empowerment and growth mechanisms public surveillance, 4) the perfection of legal and administrative proceedings, 5) improve and change the values of penalties provided by the provisions of Law Nr. 10 317 dated 16.09.2010 "On Some Additions and Amendments to Law no. 9121 dated 28. 07. 2003 "On Protection of Competition", published in Official Gazette Nr. 135 dated 07.10.2010. This law entered into force on 23. 10.2011
 12. Associated with linguistic issues I want to highlight (in a comparative overview between Albanian and community provisions) that formal changes in the text of the provisions have not gained any significance in terms of their interpretation due to the provision of

- article 71, second paragraph The SAA, which requires the Albanian Competition Authority to be based on community principles essential in interpreting the antitrust provisions. And in fact, through decisions taken by the Authority, noted that despite the fact that there are still difficulties in applying the law, which arrive as a result of the new law's age and lack of an anti-competition culture in Albania, the competition authority tends to be uniformed constantly with the best practice of the European Commission and the jurisprudence of Community Courts.
13. a) directly or indirectly fix purchase or selling prices or any other trading conditions;; b) limit or control production, markets, technical development, or investment) share markets or sources of supply; e) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage; d) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.
14. "The Provisions of paragraph 1 May, however, the EU declared inapplicable in the case of: any Agreement or Agreements between category of undertakings, Decision or any category of Decisions by Associations of undertakings, any concerted or category of concerted Practice Practices, which contributes to Production or improving the distribution of Goods or to promoting technical progress or Economic, Consumers allowing while a fair share of the resulting benefit, and which does not: (a) impose on the undertakings Concerned which Restrictions are not indispensable to the attainment of These Objectives (b) Such undertakings afford eliminating the possibility of Competition in respect of a substantial part of the Products in question. "
15. Guidelines for the implementation of Article 81 of the EC Treaty to horizontal cooperation agreements, published in the Official Journal of the European Community, 2001, C3 /2.
16. Regulation (EC) No 2790/1999 of the Commission dated December 22, 1999 on the implementation of Article 81, paragraph 3 of the Treaty to categories of vertical agreements and concerted practices, published in the Official Journal of the European Communities 1999 L 336/21.
17. The aim of the legislator in drafting the discipline of the abuse of dominant position was the elimination of monopoly positions to which consumers reduce chances of election of the products needed to enjoy their needs. Parts of Minister Arben Malaj speech during the parliamentary session for approval of law no. 9121 to 2003. The written text of a plenary session, 28.7.2003.
18. Archives of Albanian Parliament.
19. .Through law no. 10 317,16.09.2010 "On Some Additions and Amendments to Law no. 9121, 28. 07. 2003 "On Protection of Competition", published in Official Gazette Nr. 135 dated 07.10.2010.
20. The dominant position of one or more undertakings shall be determined taking into account, in particular: a) the relevant market share of the enterprise or enterprises in the review and other competitors, b) barriers to entry in the relevant market; c) potential competition; d) economic and financial strength of enterprises, d) economic dependence of suppliers and buyers; f) the countervailing power of buyers; e) the development of distribution network and access enterprise resource products; s) connections with other firms; f) other characteristics of the relevant market such as the homogeneity of the transparency of the market, cost and size of enterprises, the sustainability of demand or free production capacities.
21. It should be noted also that the European Commission proposes the definition of dominant position and on the basis of criteria which assess the dominant market position in the priorities of the Commission guidelines on implementation of Article 102 (ex 82) of the EC Treaty to the abusive behavior of dominant position by undertakings in order to exclude competitors. European Union Official Journal, February 24, 2009, C 45, section III A/11-18.
22. May constitute abuse in particular: a) establishing, directly or indirectly, the price of unfair purchase or sale, or other unfair conditions of trade, b) limiting production, markets or technical development; c)

- implementation unequal conditions for commercial operations the same parties, thereby placing them at a competitive disadvantage; d) enter into contracts, provided that the other parties to accept the additional liabilities; d) the price or other conditions that have as their object or effect the prevention of entry or expulsion from the relevant market specific competitors or a product thereof; f) refusal to deal or to license e) the refusal of entry of another undertaking, against a suitable reward, network or enterprise infrastructures with a dominant position, if this rejection of the use of simultaneous network infrastructures or other undertaking prevents act as a competitor of the undertaking with dominant position.
23. May constitute abuse of dominant position in particular: a) establishing, directly or indirectly, the price of unfair purchase or sale or other unfair conditions of trade, b) limiting production, markets or technical development; c) applying dissimilar conditions to similar actions by trading parties, thereby placing them at a competitive disadvantage; d) setting the conditions for entering into contracts with other parties, the latter to accept the additional liabilities, which to their nature or according to commercial practices, not related to the subject of such contracts.
24. This discipline is complemented by the adoption by the Authority of a series of normative acts that regulate and clarify procedures for the control of concentrations --- "Regulation on the implementation procedures of concentration between undertakings", guidance on the notification form of concentration, two types of notification form concentration, a simplified and a full, guidance for horizontal concentrations; guidance for non-horizontal concentrations and conglomerates. Regarding their content be viewed www.caa.gov.al
25. Published in the Official Journal of the European Community L. 395 Date Dec. 30, 1989.
26. Regulation (EC) No 1 / 2003 of the European Council dated December 16, 2002 for the implementation of competition rules under Articles 81 and 82 of the Treaty, published in the Official Journal of the European Community L, dated 4.01.2003
27. Ricolfi, Le concentrazioni, ne N. Abriani , G. Cottino , M. Ricolfi, Il Diritto industriale, Cedam, Padova 2001, f. 809.
28. Albanian law refers to a) the merger of two or more undertakings or parts of undertakings independent from each other, and b) gaining control, directly or indirectly, by one or more natural persons, which have both control on at least one undertaking or one or more companies, on one or more enterprise, or part thereof, through acquisition of stock, shares or assets, contract or any other lawful means, and c) control directly or indirectly over one or more undertakings or a part thereof
29. Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings, Official Journal of EC L 24/1 , 29/01/2004 article no.3.
30. The current concentrations nr.139/2004 community has modified the regulation defining the existence of risks of coordination between undertakings establishing joint enterprises to a full-function when considered concentration meets the turnover criteria specified in regulations. Profiles of collaboration during the creation of the joint undertaking are subject to an ad hoc evaluation according to the article. 2, paragraph 4 of Regulation 139/2004 TFUE under section 101 governing the discipline of prohibited agreements at Community level.
31. Council Regulation (EC) No 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation) Official Journal L 024 , 29/01/2004 P. 0001 – 0022, point 25
32. If 2 conditions are met specified in clause
33. European Commission, guidance about the assessment of horizontal concentrations. Official Journal of the European Community, February 5, 2004. In the same way are recognized the efficiencies of the increased guidelines issued by the International Competition Network (ICN Merger Guidelines, 2006) p. 61-65.
34. In reality, based on efficiency defense is used by the Community antitrust authorities before issuing the Regulation no. 139/2004 and the relevant guide lines - the European Commission's Decision, 2.10.1991, M. 053,

Aerospatale-Alenia/De Havilland. Commission evaluated negatively, although this case did not rule out the possibility of taking into account the arguments based on the concentration efficiency assessment, the European Commission's Decision, 18.10.1995, M. 580, ABB / Daimler Benz .- The Commission determined that although concentration occurred between two competing undertakings will improve the competitive situation as it will allow the two undertakings to compete better with enterprises for undertaking in a dominant position in the procurement market for the establishment of railway lines rapidly high.

35. Associated with the complex market turnover of international minimum laps down from 70 to 7 milliard, while the complex minimum turnover of enterprises in the domestic market reduced from 800 million to 400 million ALL. It also lowered the minimum turnover of at least one participating undertaking in the domestic market of 500 million to 200 million ALL.

FISCAL DECENTRALIZATION - NATIONAL AND LOCAL INTEREST TRANSFERS

ORIONA MUÇOLLARI
UNIVERSITY OF TIRANA, ALBANIA

ERIONA KATRO
ALBANIAN UNIVERSITY

Abstract

This paper reviews the Albanian situation regarding the fiscal decentralization and in details the national and local interest transfers. The past few years have constituted a period of transition for the development of the local government system, functions and financing. Policy changes have been made each year, leading to changes in the calculation of the transfers, amounts of the pool transfers and adjustment of criteria of distribution. The amount of the pool of transfers refers to local interest transfers and specifically to the pool of the unconditional transfers. In spite of the many changes, there has been a clear underlying commitment on the part of Albania's government to ensure continued increase of the funding of pool, which has often been greater than other chapters of the State budget.

Key words: local transfers, national transfers, revenue, unconditional transfers, decentralization.

Introduction

The fiscal authority and autonomy of local government is very limited. A national law defines for all local taxes and fees, the base, rate level, sanctions and collection agent. From 1999, the law established the right of the local governments to decide the rate of local taxes and fees within +/- 20% of uniform national rates decided by law. Central fiscal agents collect the majority of local taxes and fees. Few local governments have a local fiscal administration; as a result, the capacity of local governments to collect own local tax and fees remains very limited. Some large municipalities have strengthened their capacity to collect local taxes, an argument for further fiscal decentralization reform.

The National Strategy for Decentralization and Law 8652 on the Organization and Functioning of Local Governments have defined several policy objectives for decentralization of own, shared and delegated functions and the means of financing them. In addition to specific objectives as laid out in various laws and policies, there are also general criteria by which financing sources of local governments may be evaluated, as we will describe above.

Analysis and Results

Albania's system of grants has many desirable properties. The principal criteria used to distribute the grant are transparent, readily verifiable and reasonably equitable. There is a little discretion (other than in the designation of "distressed municipalities") in the measurement of these criteria. But for all the reforms that have taken place, the current system of local government transfers still has some weaknesses. First, it is unstable; and second, it is unpredictability.

The Two Components of the Local Government Transfer System

Intergovernmental fiscal transfers are an inherent element of any system of decentralized government. For purposes of this analysis we have divided such a system in two components:

Local interest transfers – those intended to assist in funding the exclusive or own functions of local governments, as defined in Article 10 of the Law on Organization and Functioning of Local Governments, and

National interest transfers – those intended to fund local expenditures to achieve national interests, such as in the case of delegated functions or compliance with minimum national standards

According to the National Strategy for Decentralization and Law 8652 on the Organization and Functioning of Local Governments it can be established that: as a rule, local interest transfers ought to be unconditional and national interest transfers conditional.

On the other hand, transfers to achieve national interests that are executed through delegation, as a rule, have a conditional nature but this does not exclude that some of the transfers for such purposes can also be unconditional.

Regarding the shared functions, the links between the local/national interest nature of the transfer vested in the given sub-functions and the conditionality or unconditionally of the related transfer is similar to the case explained in the paragraph above.

Thus, in this study instead of analyzing the conditionality or unconditionally per se we are going to analyze the system of inter-government transfers based on the concepts of local/national interest transfers.

We further will explain the difference between local interest and national interest transfers.

Local Interest Transfers

Transfers to support local governments in carrying out the functions and responsibilities in areas of local interest assigned to them by law make up the first component. Rémy Prud'homme describes the rationale for such transfers as follows :

The standard theory of decentralizations suggests that responsibilities and taxes should be decentralized jointly, and that each level of government should finance its own expenditures. This is nowhere achieved, and for good reasons. In all countries, responsibilities are more decentralized than taxes, and funds are transferred from the central government to sub-national governments. This can be done in many ways, and an intergovernmental transfers system has to be designed .

In this analysis we will refer to this component as “local interest transfers.”

In the case of Albania those transfers intended to assist in funding the exclusive or own functions of local governments, as defined in Article 10 of the Law on Organization and Functioning of Local Governments, fall clearly under the local interest transfers.

Shared local functions – those that local governments perform jointly with the central government – are a mixed case. Law 8652 provides that regarding such functions local government has its share of responsibility, distinguished from the share of responsibility granted to central government. For its share, local government has its own competencies, which are exercised autonomously . Funding provided centrally for the local government part of the shared functions falls under local interest transfers.

National Interest Transfers

There exist a limited number of issues which are of overriding national interest. These special national interests and their impacts transcend local boundaries. These are referred to as inter-jurisdictional spillovers – those cases where the benefits or the costs of the decisions made by one unit of local government “spill over” into the area of other local government units . Some examples include: air pollution; uniqueness of historical or cultural sites; valuable areas of environmental interest, such as watershed areas, etc.

They include as well all functions assigned by law to the central government. Areas of national interest would thus be established in a law.

There will be cases when the central government wants and needs to achieve these national interests through local expenditures. Transfers to fund such expenditures will have in common the fact that they respond to some degree to national interests that are reflected locally. They are the second component of the local government transfer system. In this analysis we will refer to this component as “national interest transfers.”

Funding provided by the central to local governments for the purpose of achieving national standards applicable to own functions would fall under national interest transfers.

Those transfers intended to fund delegated local functions – those assigned to a local government

for performance in a manner and to a degree that is determined by the central government – fall clearly under national interest transfers.

In the case of shared functions, should the central government seek to delegate to local governments all or part of its share of responsibility, funding for those activities would fall under national interest transfers.

Coordination of the Two Components of Local Government Transfers

Local and national interest transfers differ in their objectives, in the chain of accountability and, therefore, in the rules and procedures governing both the allocation of the transfers and the transfer of the funds. They also differ in the rules governing the calculation of the size of the transfer pool and in the manner in which fiscal policy affects that calculation.

This argues for keeping the two components separate and not commingling local and national interests in the same transfers. Doing so may make it difficult to measure and evaluate performance and obfuscate accountability. It may lead to conflicting conclusions on changes to the size of the pool in times of fiscal distress. Of course, this is a general rule that may be difficult to apply in pure form all the time.

That does not imply, however, that it is not useful to analyze the sum result of both components as they relate to individual local governments, as the total amount of funding that any given local government receives from transfers of all kinds has a bearing on its absorptive capacity and on the ability of local officials to manage and account for the funds.

General Criteria Applicable to All Transfers

Generally, there are four key criteria that are applicable to both local interest and national interest transfers: stability, predictability, transparency and equity .

Stability: Significant year-on-year changes in the overall amount of transfers do not allow local governments to plan their budgets and manage their services and activities in a rational and

coherent manner. Thus, transfers should aim to ensure stability.

Predictability: Local governments cannot manage their finances successfully or effectively if they cannot predict what their revenues will be for future years. Local governments should be able to anticipate the amount of the transfers they will receive in the current and subsequent fiscal years within reasonable bounds.

Transparency: Whatever the policy, its implementation should be through an objective mathematical formula. The formula should be used to calculate the transfer amount, without subjective adjustments. This applies to the local interest transfers as well as to some of the pools for the national interest transfers. The formula should use only data that is readily available to everyone. Also, simple formulas are better than complicated ones. The objective is to make it possible for local governments to use the formula on their own to estimate in advance and subsequently to verify the size of the transfer to which they are entitled.

Equity: Local government officials should be able to understand the transfer system, the reasons for any changes and also be able explain budget changes to the local council as well as to the public. Equity has several dimensions, including differential needs (providing more to those with greater need where the need factor includes variations in unit costs of producing public services) and differentials in the ability to raise own resources (fiscal capacity, although there is no single standard for what constitutes fiscal capacity). In fact regarding the fiscal capacity, in Albania, refers generally to the place where local commune/municipality is situated (beach or mountain), to the density of the people living, to the weather conditions and other facts .

Law 8652 on the Organization and Functioning of Local Governments establishes clearly the objectives that should guide the design of local interest transfers, that is to:

- Support implementation of own functions by closing the gap between own revenue sources and own expenditures (also referred to as vertical equalization).
- Achieve equalization of revenues among local governments (also referred to as horizontal

equalization) with the extent of equalization established by policy .

The objectives of local interest transfers provide the basis for establishing the size of the annual pool of such transfers. National fiscal policy may also influence the size of the pool. During periods of fiscal austerity, transfers to local governments may have to decrease. When fiscal conditions improve, transfers can increase .

Local governments are accountable directly to the local community that elected them for their performance in carrying out own functions. The rules for allocating local interest transfers to specific local governments and the procedures for the transfer of funds must be consistent with this all-important principle of accountability. The rules and procedures must allow local governments to exercise discretion in deciding the use of the funds, although they may provide positive incentives to local governments to exercise sound fiscal policy and discourage inefficient practices in the management of their budgets.

This means that the rules for allocating local interest transfers should be:

- Objective and, to the extent possible, quantitative to avoid subjective judgments by central authorities of local decisions regarding own functions.
- Non-distorting of local tax effort – The design should not discourage local governments in their tax creation, assessment or collection.
- Consistent with good financial management – There should be no specific transfers to finance any operational deficits of local governments.
- Applied prior to the adoption of the local budgets so that local authorities know their allocation and can weigh the tradeoffs between available revenues and planned expenditures in adopting their budget.

The process for the transfer of funds should be:

- Automatic and not conditional on the prior review by a central authority of planned expenditures in the area of own functions, although it would be appropriate for purposes of overall cash management that the central government require each local government

unit to justify the level of transfers based on a projection of its cash position.

- Treated as an expenditure of the central budget and adopted by the local authorities as a source of financing of the respective local budgets.

Evolution of Local Interest Transfers

Local interest transfers since 2001 have included:

- The “unconditional” grant designed to address both the vertical and horizontal equalization objectives of local interest transfers
- Until 2005, conditional grants to fund certain investments in own functions – replaced in 2006 with a competitive grant mechanism with the same objective
- Conditional transfers to fund urban plans and studies

National Interest Transfers

Principles - Objectives, Accountability, Rules and Procedures, Size of the Transfer Pool

The specific objectives of this component of the system of transfers to local governments will derive from central government policies and plans at any point in time. Within that context, national interest transfers have two broad objectives:

- To provide the funding required to implement the activities that local governments carry out to achieve national interests, as expressed either in central government policies and plans or national standards applicable to own functions.
- To influence overall local government budget decisions to achieve national interests.

Note that vertical nor horizontal equalization objectives do not apply a priori to national interest transfers. There are two reasons for this. First, there are no vertical gaps or horizontal differences in fiscal capacity to address because the central government must provide 100 percent of the funding for expenditures that local governments incur to achieve national interests, as expressed either in different central government policies and plans or national standards applicable to own

functions. Second, the geographic or per capita allocation of national interest transfers should be linked to the corresponding distribution of the problem or situation that the central government seeks to address, such as poverty or environmental pollution, for example. While other principles of “equity” will apply in such cases, “equalization” across units of local government may or may not apply.

In the case of national interest transfers local governments are accountable to the central government for their performance and the use of the funds. For that reason, sound practice dictates that prior to implementing such transfers, the central government prepare and disclose:

- The objectives of the transfers
- Objective criteria to measure the performance of local governments in meeting the objectives

Since local governments are accountable to the central government in the case of national interest transfers, the rules for allocating the transfers to specific local governments and the procedures for the transfer of funds may differ from those governing local interest transfers in that they may condition or otherwise limit local discretion in deciding the use of the funds. This will mean that:

- The rules for allocating the transfers should be objective and, to the extent possible, quantitative but may involve prior review by central authorities of planned local expenditures to be funded by the transfer.
- The process for the transfer of funds may be conditional on the prior review by a central authority of the status of the expenditures to be funded by the transfer.

We established that given the nature and purpose of national interest transfers, the central government must provide 100 percent of the funding for expenditures that local governments incur to achieve national interests. In order to establish the size of the pool for national interest transfers there will need to be objective criteria that provide the basis for determining the level of funding for meeting the respective national policies, plans or standards. This also means that there should not be a single pool, rather one for each separate policy objective or national standard.

In the absence of such criteria, there is no simple way to analyze the size of the pool(s). Such a situation also may lead to unfunded mandates in which the central government imposes the cost of meeting national interests on the own funds of local governments.

National fiscal policy may influence the size of the pool(s) for national interest transfers, but not necessarily in the same way that it influences the size of local interest pool. It is entirely possible that certain national interest transfers may increase in times of fiscal austerity – such as those for social assistance to address poverty or unemployment – and may decrease in times of stable fiscal conditions.

Conclusion

- In order to ensure the future predictability and stability of the transfer pool, the amount could be set as a multi-year commitment as part of the Medium-Term Budget Program (MTBP). This amount could be set, for example, as a percentage share of aggregate national budget revenues.
- Further stability and predictability will be enhanced greatly by fixing the formula one-year in advance.
- It is also important to consider that reviewing only the amount of the unconditional transfer pool and its evolution over the past years does not fully capture the increase in funding received by local governments. The introduction of the fiscal package has increased revenues from tax sharing, as well as the ability of municipalities and communes to levy and collect own source taxes and fees. This aspect also should be taken into consideration in determining, the amount of the pool and its specific source of financing.
- Funds should remain where tax revenues are created. Direct distribution implies greater risks, but also potential greater benefits, particularly where fiscal capacity is high. Tax sharing is a perfect mechanism to apply a policy goal of revenue distribution by point of origin.
- Funds should be equally distributed on a per capita basis. A per capita allocation implies no risk for local governments as the transfers are

guaranteed by the state budget. Tax sharing is not at all appropriate to ensure an equal territorial distribution of revenues, irrespective of local fiscal capacity and potential.

- Complexity versus simplicity. Part of what appears to be the complexity of the existing formula results from the implementation of specific policy goals to comply with the overall criteria and objectives of the formula: fiscal equalization mechanism; special coefficients for mountain municipality/commune and distressed municipalities; and, minimum per capita guarantee.

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POSSIBLE SELVES AND CONSUMER BEHAVIOR AMONGST FIRST TIME MOTHERS AS RELATED TO SHOPPING FOR BABY GOODS

IRIS GERTNER MORYOSSEFF
UNIVERSITY OF PECS

Abstract

This research focuses on the purchasing cycle and the consumer behaviour of first time mothers and their variance with regards to the mothers' age, education and marital status.

Many studies have examined the changes in the household structure, from the traditional family (mother, father and children) to modern family structures that include divorce, unmarried couples or single mothers.

Becoming a mother for the first time involves many aspirations, goals and fears with which they have to deal. These major changes affect the mother's possible selves.

This study examines the relationships between the mothers' anxiety level, the depth of their information search, and the evaluation phase. This relationship was tested against the status of the mother, either having a married or unmarried co-parenting arrangement with a partner, or single mothers by choice (no relationships with the child's father).

The pilot research includes 46 first-time mothers who gave birth in the last two years in Israel. The interviewees varied as regards age, level of education and marital status, and were interviewed about their consumer behaviour habits as related to baby goods such as stroller, crib, changing table or carrier.

Based on the results of these interviews, we built a model explaining consumer behaviour of first-time mothers based on the various characteristics described above.

Key words: First-time mothers, possible selves, parented mother, evaluation, shopping goods.

Introduction

Becoming a mother is a significant transition amongst Israeli women. Every year some 45,600 women becoming mothers for the first time, 8.3% of whom are single with no co-parenting relationship with a father. Most of them use the sperm bank to get pregnant (source: Israel Central Bureau of Statistics, 2008, pp 178-203)

The average age of childbearing in Israel is 26.8. The Israeli Ministry of Social Welfare passed a law in 1992 confirming a single parent is one who has a child who lives with her and

a) Is not married or have a common law partner;

b) Is married but has lived separately from her partner for at least two years and has started legal proceedings to end the connection; or is an abandoned wife; or is separate from her partner, has lived for 90 days at least in a shelter for battered women, and has started proceedings to end the connection (unless the Welfare Board determines that such a step might endanger her or her child's life;

c) Is a new immigrant, in Israel between 12-24 months, whose partner has not immigrated to Israel, and who has no other partner.

Kornfein, Weisner, and Martin (1977) classify single mothers, including mothers in their late 30s,

as independent and choosing to have a baby on their own as “nest builders”.

This paper observes the correlation between age, education and former experience with children amongst both parented and single mothers as regards their buying goods for the baby. Parented mothers were either married or in a cohabiting relationship with the baby’s father, while single mothers have no co-parenting relationship with a man and decided to get pregnant and bear a child alone.

Social and consumer studies demonstrate significant linkages between the age of the mother’s formal education, her income and marital status and the evaluation stage of baby goods purchased in terms of collecting data, the anxiety level, and the period of time she devotes to this (Kalmuss, Davidson, and Cushman 1992; Kalmijn, 1996; Lerman, 2002). It further analyzes the influence of demographic variables for a single parent and parented mothers as related to time, effort and anxiousness when starting to shop for baby goods.

The model suggested by this author shows that single first-time mothers have a higher anxiety level, spend more time before making a purchase and rely on professional data sources, compared to married or parented first-time mothers. It further refers to education as a conditional variable reducing the anxiety level both in parented and single mothers: the more educated the mother the lower her anxiety level prior to decision-making.

Literature review

Anxiety and possible selves of the new mother

Anxiety is subjective, experienced as tension and occurring in the nervous system. It is manifested as

- (1) State anxiety, experienced when something causes an appropriate and temporarily anxious feeling and then retreats until a ‘normal’ sensation is again experienced; or
- (2) As trait anxiety, which is the ‘preset’ level of anxiety experienced by an individual who has a tendency to be more anxious

Several researchers such as Hock, McBride, and Gnezda (1989), Stifter, Coulean, and Fish (1993), and Hsu (2004) measured the mother’s separation anxiety both before and after birth. Another method of measurement employs the State-Trait Anxiety Inventory questionnaire, developed by Spielberger, Gorsuch, and Lushene in 1970. Two facets of anxiety are explored therein, each with twenty items for measurement, using a State Anxiety Inventory (SAI) and a Trait Anxiety Inventory (TAI). The former measures situational anxiety while the latter measures baseline anxiety. The items are rated on a 4-point scale, with a higher score equating a greater anxiety level. Spielberger et al. (1970) find that the test retest correlation for the TAI is higher than that for the SAI. Despite the fluctuating test-retest correlations for the SAI, which reflect its validity in measuring state anxiety, the internal consistency of the SAI, as measured by the Cronbach’s alpha score, has been found to be high. The essential qualities evaluated by the STAIS anxiety scale are apprehension, tension, nervousness, and worry. The scores rise in response to physical danger and psychological stress, and drop as a result of relaxation training. On the STAIT anxiety scale, consistent with the trait anxiety construct, psychoneurotic and depressed patients generally have high scores

A mother’s anxiety regarding her first child often includes worry, sadness, guilt and fear that she cannot provide her child with his needs and will not be a good mother. The changes experienced by the new mother during the transition prior to and following the pregnancy is associated with the mother’s “possible selves identity” (Reder and Duncan, 2003; Banister and Hogg, 2006).

Pregnant women wonder about their new possible selves. “What kind of women do I want to be?” “What kind of mother do I not want to be?”

These conflicts are more substantial amongst single mothers than parented mothers due to the fact that the former are more concerned about their income ability and have less time or possibilities to adjust to their new identity and to prepare the growing new nest (Glezer, and Wolcott, 1997; Hand and Hughes, 2004).

Time as a paradigm amongst first-time mothers

Carrigan and Szmigin (2004) have found a correlation between dealing with time issues and consumption behavior amongst first-time pregnant mothers indicating that relative to their time available and income some mothers will shop around convenience stores looking for the best quality while others will bargain for low cost products.

As first time purchasers, the “good mother” is dealing with complex decisions and choices for herself and for the baby.

Carrigan and Szmigin (2004) conducted qualitative interviews with focus groups of first-time mothers in their third trimester of pregnancy on their values and attitudes when purchasing and on choices. They assert that a first baby will influence the buying process as consumption will express parental values and product usage. In their research the link between dealing with time issues and consumption behavior were based on Dapkus' (1985) three dimensions as follows:

1. Time as change and continuity (“Doing in time”): the conflict between the regular habits and the will to have a healthy diet for themselves and the new baby.
2. Time as limit and choices (“Becoming in time”): the way the expectant mother deals with time, since having a baby is a complex innovation demanding considerable time spent making purchases and seeking information before and after delivery
3. Time as tempo1 (“Pacing in time”): since pregnancy is a temporary stage expectant mothers try to use this period as best they can to collect data and information pertaining to food, clothes and others products for themselves and for the baby

Some respondents in their research adhered to the advice of experienced and informed peers, while others followed their instincts. For some of the respondents it was a choice between new items and used items from previous mothers. Many found they were limited by their financial budget, but had considerable choice and variety in baby goods. On the one hand they were overloaded with information regarding what to buy for the first baby

(from magazines, friends, and walking in stores) but on the other hand their choices were limited for budgetary considerations.

Belk (1985) and Kamineni and O’Cass (2003) show the link between materialism and the consumers’ characteristics (age, gender, education, household with one or two parents, etc.). Their studies further show that older new parents have greater difficulty adjusting to the transition than young new parents: they focus more on health care products for themselves and for the baby during the pregnancy and thereafter.

Consumer behavior of first-time mothers

Involvement can be defined as “a temporary perception of product importance based on the consumer’s desire to obtain particular extrinsic goals that may derive from the purchase and /or usage of the product” (Bloch and Richins, 1983: 72).

In this study we focus on buying goods for the baby including a stroller, crib, carrier and dresser table. All products are of high importance for the mother because of the need for them and their significance for the baby’s health.

The perceived risk felt by the new mother towards baby goods purchased for the first time motivates her high involvement and the complexity during purchasing.

Perceived risk is a popular region for researchers arising from uncertain buying as a consequence of a potential negative outcome (Dholakia, 2001).

Storey and Davies (2005) note that babies take first priority in the new mothers’ purchases, who only thereafter buy for themselves.

In their qualitative work Andersen, Sorenson and Kjaer (2008) interviewed mother’s groups in various provincial cities (small, middle and large) on their consumption behavior of baby’s clothing from supermarkets and premium brands. The findings show that the mother’s purchases of clothing indicate the extent of good mothering. Thus a perfect mother will buy designer products, and a less good mother will purchase goods from the supermarket.

These findings support the assumption that purchasing baby goods, even if at the expense of

the mother's purchases, affect her self-image as a mother.

Demographic characteristics of first-time mothers

Family status

In recent years the number of single mothers 2 in Israel increased three-fold compared to the last century (Israel Central Bureau of Statistics, 2008:178-203). The number of single mothers by choice is also increasing globally (Wolfinger, 2008). In Iceland 63% of the new births are by single mothers, in Denmark it is 50%, in Norway 54%, and USA 43%. In 2007, 14% of the mothers in Israel were single mothers with no co-parenting relationship.

Most of the single mothers (64%) were born in Israel, have a higher education (72%), and work in a full-time job (75%). The average age of the first birth

among single mothers is 36.1 years compared to parented mothers who averaged 27.1 years of age.

Being a single mother is a stressful transition in the family life cycle and a critical decision for the parent. Since the period of childbirth can be longer and postponed before embarking on a career, many women do not want to wait for Mr. Right, and the alternative to being a single mother is neither rare nor uncommon (Hill, 2009).

The new family life cycle concludes the stage of being a single parent.

The literature on single parent households notes the work overload

experienced by them but offers little empirical evidence for a difference in the contribution to household production between one parent and two-parent

frameworks. Sanik and Mauldin (1986) observe that single parents suffer strong social and emotional consequences due to the absence of a spouse, and bear all the responsibility for homemaking, child care and employment. Researchers find that single mothers have little or no time to relax after working all day, while Schlesinger (1977)

discusses the social isolation and loneliness of single parents.

Age

A review of the literature concerning age and the transition to motherhood indicates that age has a crucial influence on stress amongst first-time mothers (Bouchard, Mylene, and Amanda, 2008)

Research, in general, shows that in recent years more women are choosing to delay motherhood not only because they have not found their desired partner but also because they have other alternatives for self-fulfillment prior to childbirth. These characteristics are shared by most older first time mothers (after the age of 35), with a high educational level (76.4% of the older mothers have higher education), a professional occupation, who are career-focused and have often made a career move to a distant capital (Merlo 1995; Weston, Soriano and Qu, 2006).

Teenage mothers, with a socio-economic disadvantage, present the opposite attributes – they are young, have often barely completed high school, and lack financial assets.

Young mothers (up to the age of 35) are more concerned about their financial savings and abilities to provide regardless of their family status, while mature mothers (in their late 30s) whether single or partnered, face the "Maternal wall" (Swiss and Walker, 1993). The barriers combining career and motherhood are likely to be a big challenge for the mother trying combine work and motherhood, but research amongst first-time mothers shows that they postpone motherhood for many years, but are then are dedicated to being a mother and stay at home to care for the baby. They have more saved income, squander less, and are more aware of saving and of financial security for themselves and the newborn compared to younger parents (Chi-Ching, 1995; Powell and Powell, 2001).

Single parenting entails far more financial stress than for parented mothers, who will return to work much faster than the latter. Mature-aged mothers are more rational, since their decision-making and preparation is different, and they are more prepared for motherhood than young mothers (Bouchard et al., 2008). Furthermore, older partnered or single mothers will be more prepared and less worried than young single and partnered mothers

The ability of mature-aged mothers to adjust to changes compared to normative aged mothers is discussed in other studies (Hall, Wulff, White, and Wilson, 1994; Kapinus and Johnson, 2003; Campbell, Lackenbauer, and Muise, 2006).

Education

Education as a prejudiced character for mothers' behavior has been studied in the literature, which shows that mothers with a post high-school education focus on buying educational goods for the baby, notably books, educational toys and didactic games (Krein and Beller, 1988; Kalmijn, 1996).

In the child's early years the mother has a greater impact on the child's education than the father, while in high school the influence is the same (Krein and Beller, 1988).

Bronfenbrenner's ecology model (1979, 1986) implies a link between mother's education, the household framework and consumption.

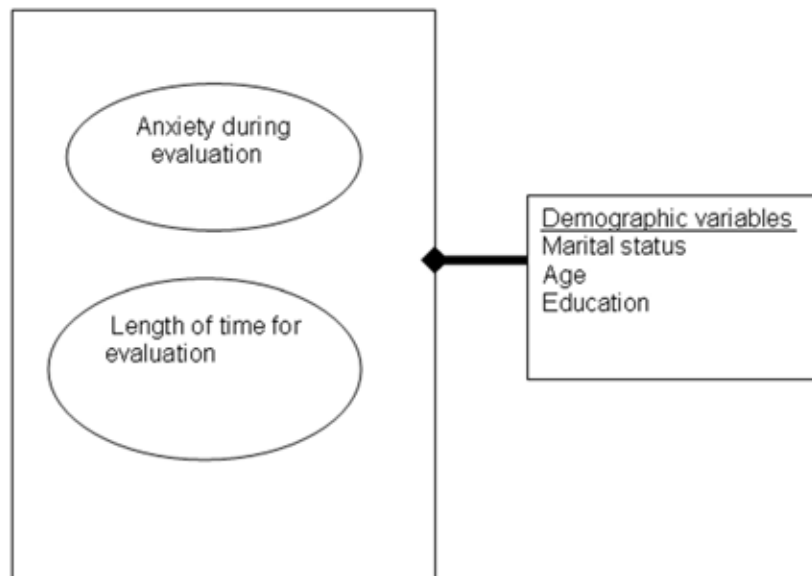
Households with two parents who have a post-high school education invest greater sums of money in formal and informal educational consumption, and focus on creating a separate and quiet environment for the child to learn and play (Bronfenbrenner, 1986).

This paradigm matches the research by Goodnow and Collins (1990), who suggest that married first-time mothers with higher education will buy more didactic games, books, and educational goods compared to other first-time mothers.

The suggested model

Based on the literature review the author proposes the following model predicting the mother's consumer behavior, based on family status, age, education and income.

Conceptual model of first-time mothers and demographic characteristics



Hypothesis 1

Single first-time mothers have a higher level of anxiety during purchasing shopping goods for the baby than parented first-time mothers.

Because of the importance of family status in related consumer behaviour and the global

increase in single mothers it will be interesting to explore the correlation between family status and the anxiety level regarding shopping goods

Hypothesis 2

Single mothers will spend more time in consumption behaviour shopping for baby goods than parented mothers.

Based on the literature review dealing with consumer behaviour it will be interesting to explore the amount of time spent in consumption behaviour for baby goods relative to family status.

Data and methods

Sample

The research was based on personal interviews with 46 mothers in baby health care in Israel between October 2010 and January 2011.

The dependent variables were mother's age at the time of the first birth, education and family status. The sample embraces 20 single mothers and 26-parented mothers, all of whom gave birth in the last two years. Sixteen of the first-time mothers were aged 18-24, twenty-three mothers were aged 24-35, and seven mothers were aged 35-44. Twenty-one mothers lacked higher education, and 25 first-time mothers had a higher education.

Table 1 presents a profile of the key demographic characteristics of the sample.

Measurement

Anxiety: This dependent variable was measured using the State-Trait Anxiety Inventory questionnaire, developed by Spielberger et al. (1970), and presented in the review of the literature.

The amount of time spent by the mothers searching for baby goods is measured through questions that included how much time they spent seeking information prior to purchasing and how much time they actually spent purchasing.

Control variables: The mothers' age of transition to motherhood, education and family status were measured using demographic questions referring to each variable. Age was categorized as 24-34 and 35-45; education was classified as low (up to high school) and high (post high school) education and family status was a single or parented mother.

Results

First, total scores were calculated on the anxiety scale for each participant and for each of the scales regarding the subjective duration of the time allotted for searching for baby items and the objective duration of time allotted for searching baby's items. The total scores for all the scales were calculated as the mean of all the items in the relevant scale. Thus, a high total score on the anxiety scale reflected a high feeling of anxiety. A high total score in the subjective and objective search time scales reflected a lengthy search. In order to calculate the total score for the extent to which the participant consulted professional others regarding baby items, the first item in this scale (i.e., "consulted with my partner") was omitted. The total score was therefore calculated as the sum of the remaining items in this scale, thus a high score reflected a high tendency to consult with professional others. We now turn to examine the research hypotheses.

Hypothesis 1: Single first-time mothers have a higher level of anxiety during purchasing shopping goods for the baby than parented first-time mothers.

To this end, we first examined whether there are demographic factors correlated with the levels of anxiety. Pearson correlations revealed that levels of anxiety were correlated with years of education, $r = -.38$, $p < .01$, such that less educated mothers reported higher anxiety than educated mothers. Levels of anxiety were also correlated with the level of family income, $r = -.31$, $p < .05$, such that mothers from low-income families reported greater anxiety than mothers from high-income families. Therefore, in order to prevent a possible distortion, these two variables were controlled in the examination of the first hypothesis. In order to examine the difference in anxiety levels between parented and single mothers a one-way ANOVA analysis was conducted, with marital status as the independent variable, anxiety as the dependent variable, while controlling education and family income. As predicted, the anxiety level of single mothers ($M = 2.58$, $SD = 0.49$) was slightly higher than the anxiety level of parented mothers ($M = 2.33$, $SD = 0.38$). This difference was significant, $F(1,42) = 4$, $p < .05$, thus confirming our hypothesis.

Table 1: Sample characteristics

	Single mothers	Parented mothers
N	20	26
Age (years)	M= 32.9 SD= 4.58	M= 33.78 SD= 5.65
Baby's age (months)	M= 11.22 SD= 4.50	M= 9.23 SD= 5.86
Education (number of years)	M= 16 SD= 2.47	M= 15.38 SD= 1.17
Income below average	21.1%	17.4%
Income average	68.4%	73.9%
Income above average	10.5%	8.7%

Table 2: Means (and SDs) of the subjective and objective durations reported as a function of marital status

	Single mothers	Parented Mothers
Subjective duration	1.93 (0.86)	2.13 (1.02)
Objective duration	2.32 (0.99)	2.17 (0.75)

Hypothesis 2: Single mothers will spend more time in consumption behaviour shopping for baby goods than parented mothers.

This hypothesis may be divided into two secondary hypotheses. In the first secondary hypothesis, the time allotted for searching for baby items was measured by the subjective duration. In the second hypothesis, the time allotted for searching for baby items was measured by the objective duration. Descriptive statistics are presented in Table 2.

The data presented in table 2 suggests that whereas for the subjective duration, mothers spent more time searching for baby items than single mothers (in contrast to our prediction), the opposite pattern was found as predicted for the objective duration.

Each of these differences was put to an independent-samples t-test analysis. The difference between single and parented mothers

in the estimates of the subjective duration of time was not significant, $t(44) = -0.74$, ns., as was the difference between single and parented mothers in the estimates of the objective duration of time, $t(44) = 0.57$, ns. Therefore, the second hypothesis was refuted.

Discussion and limits

One of the most basic events in a woman's life is the transformation generated by giving birth. The internal and external world changes irrevocably as the new personality experiences profound adaptation to the baby's needs. Throughout history women have devised strategies, and sometimes adopted rites, devised by other more experienced women, to aid them in this process. The need for support reflects the consciousness of the issues associated with birth, including the risk of infant and maternal mortality. Despite the low level of threat to the infant's and mother's wellbeing due to

modern obstetric care, the worry and concern still exist for all parties.

Based on the findings of this study we can see that parenthood emphasizes the financial attention to expenses, income and saving. It increases the disagreements between new fathers and mothers as to whether they can support and provide for the baby's needs. Will they be able to save money? Can they manage the financial burden of a child? New parents become more aware of their expenses, income, saving assets and so on in the past and currently. They find themselves forced to adopt more reasonable buying habits that may entail postponing large expenditures (such as car, electrical goods or even moving house) and first consider buying goods for their first baby rather than themselves.

The study suggests that being a first-time mother, in a co-parenting relationship, reduces the anxiety over consumption of high involvement goods for the baby, probably because the parents consult among themselves and make the decisions after evaluation and discussion. First-time single mothers must take decisions regarding another person all alone, bearing all the responsibility by themselves (Halle, et al., 2008).

Fathers play a significant role in the transition to a family with a new born baby by supporting and participating in the child's development as early as during pregnancy (ibid). Single mothers have the same obligations towards the newborn but must cope with the new person in their life on their own.

The study also shows that new mothers do not spend different amounts of time according to their family status. Both single and parented mothers use their time as needed to evaluate and estimate baby goods prior to making a decision.

The complexity of the transition to first-time motherhood raises many questions such as what references and data sources are used by the new mothers and what significance is related to each source? What other demographic variables influence the new mother's consumption behavior? What is the percentage of e-purchases relative to data sources for single versus parented mothers. Other questions that should be studied are the differences between single and parented mothers in their behavior after buying the baby's goods, and their evaluation after purchasing. Finally more

research should be conducted into the nature of the decision process amongst new mothers relative to their income and previous experience with babies. The increase in the number of single new mothers makes it potentially viable, from the baby's point of sales, to have an improved marketing strategy to adjust goods and performance of an exclusive orientation to this niche and thus fulfill its needs completely.

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ANTECEDENTS OF DOCTORS' PURCHASE INTENTION FOR INNOVATIVE PROFESSIONAL SERVICES: DIFFERENCES BETWEEN COMMERCIAL AND EDUCATIONAL SERVICES

RIZOMYLITIS IOANNIS
KOSTOPOULOS GIANNIS
KOSTANTOULAKI KLEOPATRA

Abstract

The present paper seeks to investigate the factors that influence doctors' purchase intention for supplementary professional services that have been recently introduced to the market and how these factors alter accordingly to the nature of the services. For that reason a theoretical framework has been developed and empirically tested using data collected from 100 doctors. All doctors were personally interviewed with the use of a structured questionnaire. In order to explore for potential differences depending on the nature of service, two different cases of services were used: a commercial service (e-detailing) and an educational one (on-line training).

The results of our study indicate six factors that influence significantly doctors' intention to buy the addressed services. Three of them derive from the technology acceptance theory and the TAM model (perceived usefulness, ease of use and professional image) while the rest refer to the doctors' professional characteristics (work experience, current employee status, and familiarity with the on-line context). Another important conclusion of the present study is that the influence of the aforementioned parameters on doctors' purchase intention is different for the two kinds of services. These differences also imply that perhaps alternative marketing approaches are suitable for the two service contexts.

Keywords: Innovative Services, TAM model, Medical Services

1. Introduction

Innovation has been long been consider an important pursuit for companies that offer online services. Particularly for professional services innovation is a major source of competitive advantage for both the provider and the buyer (e.g. Bharadwaj et al, 1993; Chapman et al, 2003; Kandampully and Duddy, 1999). Predicting the adoption rate of an innovative service can be a real hazard for service providers. For many years, academics have attempted to put light on the factors that determine the potential buyers' behavioural intentions. Most of the ongoing research is based on the Technology Acceptance Model (TAM) a theoretical model that was firstly introduced by Davis (1989). During the past three decades a growing number of researchers from the fields of marketing and information systems have explored a wide variety of innovation adoption predictors in different contexts and for different types of potential users (e.g. Jeyaraj, Rottman and Lacity, 2006; Venkatesh & Davis, 2000; Gefen and Straub, 1997; Kimberly and Evanisko, 1981).

Some of these studies have explored the case of doctors as professional users (Mitchell et al, 1996; Chau & Hu, 2002; Yi et al, 2006). However to our knowledge, there is no study combining technology acceptance variables with variables regarding doctors' professional characteristics. To this aim, the present study seeks to make a contribution by developing and testing a theoretical framework that integrates variables deriving

from TAM with specific physicians' professional characteristics. Specifically, as shown in figure 1, in our conceptual framework we have included six potential predictors of doctors' purchase intention: perceived usefulness, perceived ease of use, professional image, familiarity with the online environment, work experience and work status. Finally, the second important contribution of our study is that it incorporates the moderating role of the service's nature (commercial, educational) to the aforementioned relationships.

2. Literature Review

2.1 Technology Acceptance Model and Physicians Behavioral Intentions

Since it was firstly introduced to the literature (Davis, 1989; Davis et al, 1989) the Technology Acceptance Model (TAM) explained the behavioural intention to use (purchase) a technological innovation using two primary predictors: Perceived Ease of Use and Perceived Usefulness. Perceived ease of use is defined as "the degree to which a person believes that using a particular system would be free of effort" whereas perceived usefulness refers to "the degree to which a person believes that using a particular system would enhance his or her job performance" (Davis, 1989, pp. 320). In the next two decades many researchers attempted to refine the proposed model by testing the significant influence of the two major predictors in specific contexts (e.g. Hu et al, 1999) and by proposing several other variables as predictors of a potential user's intention to adopt a technologically innovative product or service (King & He, 2006). Among other, these factors include attitude towards technology, perceived behavioural control, prior use, social influence and many others (e.g. Jackson et al, 1997; Igbaria et al, 1997; Venkatesh & Davis, 2000).

In the pertinent literature, there are several studies examining factors deriving from TAM that predict physicians' intention to use innovative services (e.g. Mitchel et al, 1996; Yi et al, 2006). Apart from the two major predictors (perceived ease of use and perceived usefulness) in the specific context, previous researchers have also tested the influence of subjective norms such as the perceived professional image of the potential user (Chen et

al, 1998, Chau & Hu, 2002). According to Chau and Hu's findings, the path from subjective norms to behavioural intention was not found significant because a physician is rarely influenced by other people's opinion as he/she usually develops easily a professional opinion of his/her own. However, this conclusion is based on a research that used telemedicine as a case of innovation. In the present study proposed cases of technological innovation refer to commercial and educational online services. Therefore, we argue that as doctors do not have the same degree of expertise in such services subjective norms (as perceived professional image) may influence significantly their purchase intention.

Based on the above discussion, we formulate the following three research hypotheses:

H1: Perceived ease of use influences positively a doctor's intention to adopt innovative on-line services.

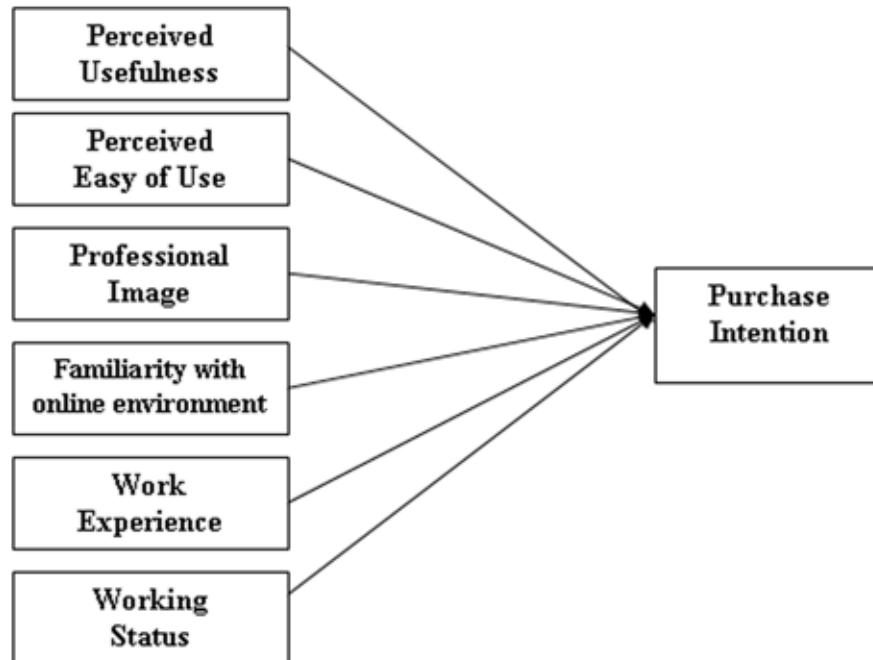
H2: Perceived usefulness influences positively a doctor's intention to adopt innovative on-line services.

H3: Others people perceptions on a doctor's professional image influences positively his/her intention to adopt innovative on-line services.

2.2 Professional Characteristics

Apart from the antecedents of doctors' purchase intention deriving from the TAM model, in the present study we also explore the influence of doctors' several professional characteristics. The reason why we believe that it is necessary to integrate these variables in our research is that doctors behave differently than other business managers when purchasing products and services regarding their profession and especially innovative ones (Chau & Hu, 2002). Specifically, doctors tend to be technologically non-competent but at the same time highly educated and very capable in learning new things (Mitchell et al, 1996). On this basis, we argue that doctors that are more familiar with the online environment will be more likely to purchase on-line products and services and particularly innovative ones.

Figure 1: Conceptual Framework



At the same time, doctors usually are very confident on their knowledge and skills and hence very reluctant in adapting new ways of working (Anderson & Aydin, 1997). Moreover, they are professionals that have great autonomy both in their work and in any purchase regarding their profession (Chau & Hu, 2002). These characteristics become more intense as doctors become more experienced and their working status changes. Hence, it is logical to assume that in the case of innovative online services, doctors with greater work experience and an upgraded working status will be more reluctant in adopting such services.

On the basis of the aforementioned discussion we formulate the following research hypotheses:

H4: A doctor's familiarity with the online environment influences positively his intention to adopt innovative on-line services.

H5: A doctor's work experience influences negatively his intention to adopt innovative on-line services.

H6: A doctor's working status influences negatively his intention to adopt innovative on-line services.

2.3 Moderating role of the service's nature

As described above, physicians' intention to adopt an innovative online service is significantly influenced by their professional characteristics. This influence however is highly possible to differ for educational services and commercial ones. According to the pertinent literature, consumers' motives and criteria are completely different when they purchase educational services (DiDomenico and Bonnici, 1996). In the case of physicians' online purchases, it is reasonable to assume that doctors are more involved when buying training and educational services than commercial services.

Previous research has shown that high levels of familiarity with the context lead to greater purchase involvement (Zaichkowsky, 1985) especially in the online environment (Rodgers et al., 2005). Moreover, more experienced doctors as well as doctors working in the private sector are also more involved with the purchase of educational services than less experienced doctors and doctors working in the private sector. Thus, doctors' professional characteristics such as experience and working status might have a stronger influence on their involvement and therefore their intention to buy

educational services rather than commercial ones. On the basis of the above discussion we formulate the following research hypothesis:

H7: The influence of a doctor's personal characteristics on his intention to adopt innovative on-line services is different for educational and commercial services

3. Methodology

3.1 Sampling and Data Collection

In order to empirically test our research hypotheses we conducted a field research, approaching physicians at their working environment. In total, we contacted 252 doctors, of whom 100 agreed to participate in our research, deriving hence a response rate of 39.6%, which we consider very high given the special nature of our sample unit. All doctors complete a structured questionnaire in presence of a fellow researcher. Regarding the demographic characteristics of our sample 66% of the respondents were males and 34% females. The sex proportion of the sample is similar to the proportion in the population of doctors in Greece, enhancing thus the representativeness of the sample. The average age was 41, while the average working experience was 12.4 years.

3.2 Operationalization of Variables

Regarding the instruments used to capture the constructs we included in our conceptual framework, where possible, we used formerly tested scales. In order to measure perceived usefulness, ease of use and professional image we used scales developed and empirically validated by Davis (1989), using Likert type items with anchors 1-7. The possibility of purchasing the proposed online services also addressed through a single item scale which asked "How possible do you consider using the described service in the next 12 months". All questions were addressed to the respondents separately for each service

(educational, commercial). Hence the responses for the two groups of questions are described as nested within the subject (respondent). Finally, the professional characteristics of physicians were measured directly, using single item scales. Specifically, for the measurement of physicians' familiarity with the online environment we used the following question: "How familiar are you with the use of internet for professional reasons" with anchors 1-7. Professional experience was measured objectively by the years of the doctors' employment, whereas working status describes whether a doctor is currently employed in the public or the private sector.

Confirmatory factor analysis (CFA) was employed (Table 1) in order to examine unidimensionality and discriminant as well as convergent validity of the three multi-item scales we used. As can be seen from Table 1, the measures were proven to be unidimensional and valid in terms of discriminant and convergent validity. All measures were also examined for internal consistency as reflected by construct reliability, which was assessed through Cronbach's α .

4. Analysis and Results

4.1 Antecedents of Purchase Intention

To check the validity of our research hypotheses, we constructed a hypothesized model and followed a confirmatory approach, checking the significance of all causal relationships within it. For this purpose the most appropriate analysis is Structural Equation Modelling (SEM). Due to sample size limitations the analysis was carried out only for the path model.

The results of the Goodness-of fit test of the hypothesized model show an excellent fit of the hypothesized model to our data as indicated by the values of the most common used fit indices: a CFI of 0.961, a TLI of 0.954 and RMSEA of 0.07.

Table 1: Confirmatory Factor Analysis, Reliability, Validity

Constructs	CFI	TLI	RMSEA	AVE	Cronbach a
Perceived Usefulness	0.931	0.922	0.088	0.64	0.78
Perceives Ease of Use	0.946	0.933	0.070	0.59	0.85
Perceived Professional Image	0.912	0.905	0.080	0.63	0.88

Table 2: Fit Indices and Path Coefficients

CFI	TLI	RMSEA			
0.943	0.920	0.070			
Path Model			Standardized Beta	T	Sig.
Perceived Usefulness	→	Purchase Intention	1.511	3.122	< 0.05
Perceived Easy of Use	→	Purchase Intention	3.059	6.480	< 0.05
Professional Image	→	Purchase Intention	1.872	3.444	< 0.05
Work Experience	→	Purchase Intention	1.586	3.344	< 0.05
Working Status	→	Purchase Intention	0.992	1.493	> 0.05
Familiarity with Internet	→	Purchase Intention	1.773	3.456	< 0.05

According to the results of the significance tests for the coefficients of the path model (Table 2), purchase intention is positively and significantly influenced by all three variables deriving from TAM (Perceived Usefulness, Perceived Ease of Use, Professional Image) which is consistent with the results of previous studies on this subject. The influence of work experience and the familiarity with the online environment on purchase intention was also found positive and significant as expected. On the contrary, the influence of the doctor's working status was not found to significantly affect purchase intention. This means that the possibility

of a doctor adopting an innovative on-line service is the same for doctors that work both in the private and the public sector.

4.2 Moderating Role of Service Type

In order to check for the three hypothesized moderating effects we carried out three Hierarchical Moderated Regression Models. For each model, one of the three professional characteristic and its interaction with the variable identifying the service type were used as independent variables. Doctors'

purchase intention was used as the independent variable, in all three models. This technique is commonly used for checking moderating effects, as the bias that occurs is minimum when the reliability of all the scales used is high (Berens, et al., 2005).

The tests for the significance of the interactions (Table 3) indicate a significant effect of the service type on the relationships of purchase intention with work experience and online familiarity. Specifically, according to the results the influence of work experience and the familiarity with internet is stronger for the educational services. On the contrary, the moderating effect of the service type on the relationship between working status and purchase intention was not found significant.

4. Conclusions and Managerial Implications

The emerging results lead us to some very interesting and important conclusions that may be useful to the marketing managers or executives. First of all, results show that TAM model can actually find applications in professional purchases / contexts as well. This means that marketers can put their efforts towards emphasizing the perceived ease of use and the perceived usefulness of these products when promoting innovative products to professionals like doctors. By underlining these aspects of the product they can have greater chances to get positive results with respect to achieving a purchase.

On the other hand doctors having an upgraded working status seem to be reluctant in adapting new ways of working probably due to their knowledge – based confidence and skills (Anderson and Aydin, 1997) which in turn lead them to be skeptical and egocentric in any purchase regarding their profession (Chau and Hu, 2002). This is something that managers should have in mind when designing the promotion of products addressed to doctors in order to avoid following wrong directions. For instance, innovative online services should better be promoted to new entry doctors since, according to our results, doctors with greater work experience

and higher working status are expected to be more reluctant in adopting such services. Consequently, establishing specific and measurable promotion goals based on TAM model prior to the promotion campaign is of major importance for managers promoting innovative product to doctors, given the fact that they can then have a substantial evaluation of the outcome.

There are, also, some characteristics that seem to have great impact on doctors' purchase intentions. In particular, doctors' familiarity with the online environment appears to be a crucial factor having positive effect on the way doctors' deal with their buying decisions. This is normal, since online services adoption demands an increased level of adaptability and familiarity.

Moreover, other people's perceptions on a doctor's professional image tend to positively affect the decision of a doctor to use online services in his work. That means that doctors are expected to adopt innovative on-line services in order to enforce their image when their customers consider them to be prestigious. The specific profession has always been highly prestigious and as such all elements enforcing a doctor's image is considered to be of major importance. Hence, innovative on-line services, which constitute by default an indication of positive image, tend to be adopted by doctors that are considered to have a high standard professional image. So, managers can underline the prestigious aspects of a potential adoption of innovative on-line services when addressing their promotion to doctors.

In sum, this study strengthens previous research findings regarding the delicate balance to be achieved between the factors that determine the potential buyers' behavioural intentions. Executives and researchers ought to clarify and assess the way professionals deal with buying procedure when it comes to adopt an innovative service in order to get an integrated perspective of the dynamics of innovation in professional services.

Table 3: Significance Tests for Moderating Effects

MODERATING EFFECT	STANDARDIZED BETA	T	SIG.
Work Experience X Service Type	0.544	5.454	.000
Working Status X Service Type	0.179	1.107	.264
Familiarity with Internet X Purchase Intention	0.642	6.837	.000

5. Limitations and Suggestions for Further Research

Although it offers useful conclusions for academics and practitioners, our study is tempered by several limitations. First, this study uses only one example of each type of service (online training and e-detailing). Future research should use more examples for each type of service in order to ensure the accuracy of our finding. Moreover, our study was conducted in a single national and cultural context. Any further research on the subject must take into account this limitation and validate our findings in other cultural environments. The third limitation lies in the sample size of our study. Although the sample size of 100 subjects is acceptable for the analyses used it can be viewed as relatively small.

Further research should also investigate the influence of other factors of the Technology Acceptance Model as well as more professional characteristics, such as self-efficacy, prior similar experience, resistance to change etc on physicians' intention to purchase online professional services. Finally, an interesting subject for future researchers could be the identification of the variables that determine perceived usefulness, perceived ease of use and professional image as in previous researches in different contexts.

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EFFECTIVE METHODOLOGY FOR THE RESEARCH AND CRAFTING OF CULTURAL SPECIFIC CASE STUDIES

SCOTT KENNETH CAMPBELL
AUBURN UNIVERSITY AT MONTGOMERY

Abstract

The inclusion of use of case studies is a long and well accepted component in many educational settings. Case studies can vary significantly in their focus, orientation and methodology. However, a common observation with the use of case studies is the fact that many of the available case studies tend to have a western cultural focus in both the topics addressed as well as the solutions proposed. In this article, the author seeks to identify some practical steps and methods for the research and craft of case studies appropriate to specific cultural areas and situations.

Keywords - Case Study Research, International Application, Business Research, Business Education

Introduction

The use of case studies in the classroom is an established procedure to prepare students for some of the situations they will encounter when they have graduated and enter the workforce. Cases help describe and explain certain phenomena that relate to people, groups, organizations, communities, large towns or even countries. Such phenomena can include leisure time activities; the treatment of an ADHD child; the determinants of individual health; the way in which people use their social network; how people cope with a disaster; riots; strikes; the process of adoption of an organizational innovation in a hospital; the principles according to which political coalitions are formed; or, an arms' race between nation-states (Michael, 1999). Research, (Burbach et al., 2004; Popil, 2011; Tusi, 2002), has indicated that the use of case studies in courses leads to an increase in critical thinking skill by the students. Lisa Tusi, (2008), stresses

that critical thinking is the ability to identify issues, recognize important relationships, evaluate the evidence and make the necessary inferences necessary to come to conclusions about the situations presented. Kunselman and Johnson (2004) stress that case studies provide students with a variety of important skills such as critical reasoning, analytical skills and problem solving experience. All of these skills are valuable when the students leave the classroom and enter the workforce. In addition, using and developing case studies can be beneficial to the instructors as well. Developing and using case studies can help keep the coursework fresh and current. They can help keep the instructor motivated by introducing new and interesting material into a tried and true class (Kunselman and Johnson, 2004). Cases studies can roughly be divided into two general types: extensive approaches and intensive approaches (Michael, 1999).

Extensive Approach

In an extensive approach, the author collects information about the relevant properties of a large number of instances of a phenomenon. Conclusions are drawn by putting together all the information and calculating and interpreting correlations between the properties of these examples. For instance, in a study about the conditions for and causes of riots (the phenomenon under study) the author may start by making an inventory of, say, 200 riots using documentary sources. Factors, such as the number of people involved, the extent of damage to property, the weather conditions, and correlations between these properties can be reviewed in order to construct a model of causes and consequences.

In extensive research, the author uses a large set of events, people, organizations or nation-states to draw their conclusions about the phenomenon being studied. In sociology, in the political and educational sciences, as well as in several other disciplines, large-scale surveying of people is the dominant extensive strategy to collect empirical data. Hundreds or even thousands of respondents may be involved to study a phenomenon. This might, for instance, be the causation of smoking habits in individuals. Each survey respondent provides information in the form of answers to a series of standardized questions. These answers are not used to study the development of the phenomenon within this individual person. They are aggregated over all respondents to create information about frequency distributions and relationships between the variables under study which might be helpful in understanding and explaining the phenomenon (Michael, 1999).

Intensive Approach

In contrast to the broad, large scale process used for extensive case study research, when in applying an intensive approach, a researcher focuses on only one specific instance of the phenomenon to be studied or on only a handful of instances in order to study a phenomenon in depth. The author would study some riots, or some young people, or some traffic accidents, or only a handful of schools by probing into the details of the process (they are interested in researching). Each instance is studied in its own specific context, and in greater detail than in extensive research. Data is collected using many sources of information, such as spokespeople, documents and behavioral observations. There are not only many separate variables to measure, but a phenomenon is also followed over time by repeatedly measuring some of these variables. This explains the label 'intensive'. Monitoring helps the author to describe and explain the history, the changes during the period under study and the complex structure of the phenomenon.

Discussion

In selecting more than one case, the usual procedure is to design a tentative model based on the results of the first studied case, and to adjust the resulting model when and where necessary while studying the other cases, until the designed

model fits all cases. Alternatively, we may discover that different models are necessary to fit different cases, depending on certain conditions. But, the focus is on the description and explanation of developments within one case.

Evidently, an intensive approach may provide us with tentative ideas about the social phenomenon, based on knowledge about the studied event or about this specific person, organization or country, and 'how it all came about'. That is to say, a case study is an appropriate way to answer broad research questions, by providing the readers with a thorough understanding of how the process develops in this case. Whether its results can be generalized in other contexts, remains an open question, to be answered by complementary case studies and/or an extensive approach (Armisted, 1984).

Phenomena and cases

In a case study on the causes of traffic accidents, (involving pedestrians e.g. pedestrian/motor vehicle collisions) we may, for instance, select from documentary sources of, say, ten accidents that occurred within the boundaries of a selected city. Cause within this specific type of traffic accident constitutes the phenomenon, and the ten accidents constitute the (ten) cases. Within the study, of each accident, the regulations and specific features of the local situation as well as the characteristics of the participants involved and the actions of the local police are taken into consideration. In another example – a case study about fatal decisions on battlefields (the phenomenon) – the study may consist of an intensive analysis of documents concerning some fatal decision in five great battles (the five cases) in the Second World War.

A phenomenon may involve only one actor, such as in a study about the trajectory of terminal illness in one individual person. In other examples, such as in studying the development of friendships in a classroom, a riot or an industrial merger, each case or manifestation of a phenomenon may often involve many individual as well as collective actors. Hence, a case does not necessarily involve only one 'actor', such as a person, an organization or a local settlement. Depending on the phenomenon of interest, the actors involved in a case may be located on the micro-level (persons and interpersonal relations), and/or the macro- (organizational, institutional) level (Boyce, 1993).

Micro-level, focusing on one actor

For example, the clinical research, such as description, diagnosis and monitoring the treatment of individual patients; or historical research such as biographies of famous politicians.

Micro-level, more than one actor involve:

For example, people in a restaurant; some people together in an elevator (the phenomenon might be how people bring a conversation to an end or the continuous adjustment of physical positions in the elevator).

Macro-level, only one actor

The example of a macro level including only one actor, can be of an organization, such as a firm or a department; a police station; a hospital; a voluntary association.

Macro-level, more than one actor involved

For example, co-operations or networks, such as between four local primary schools and a school for special education; conflicts between public service and private enterprise in the renovation of an inner city; co-operation of industrial firms and educational institutions with respect to the labor market and learning places.

A combination of micro and macro level actors

The combination of micro and macro level actors can be understood by the example of socializing newcomers into an organization.

By far the most popular branch of case studies relates to organizations. Substantial fields where case studies are used include marketing, human resources management, management information systems and strategy. The intensive approach, it also shares common ground with the scientific tradition of experiments. It belongs to the broad category of evaluation research, and nowadays is undoubtedly the most popular branch of applied research. In evaluation research, both extensive and intensive approaches are used. Nonetheless,

in the fields of psychology, psycho-therapy and medicine, the label 'case study' is generally used for this kind of research. In this book, this micro-level tradition is not where our main interest lies. Rather, for readers wishing to pursue this tradition (Michael, 1999).

On a macro-level, the dominant tradition is represented by those case studies in political science and the economy, in which, certain phenomena (i.e. peasant revolutions, wars) are connected to a restrictive set of causative 'hard' variables, such as population size, climate, economic development or armament level. An exemplary study might be about the impact of electoral systems on the number of parties in a country. Data is obtained from documentary sources. The political sciences and economics traditions stand apart from the case study tradition in sociology, the administrative and management sciences, health- and social care sciences, and most other disciplines (Michael, 1999).

A more appropriate expression would be that a case study is the study of a phenomenon or a process as it develops within one case. The point needs to be emphasized, particularly where only one actor (person, organization or local setting) is involved. In intensively studying the medical history of a person, or the development of some public service, sometimes the researcher's attention gradually shifts towards this specific, selected person, organization or nation-state, while the phenomenon in general more or less remains backstage.

Implication of Case studies

The growth and development of many sciences, such as the health sciences, clinical psychotherapy and law, went hand in hand with the study of cases. Description and attempts to explain the peculiarities of a case proceed, or are part of, steps towards generalization. In the teaching of these disciplines, cases still play an important role as a didactical vehicle. A similar orientation on cases can be observed in fields that developed later on, such as political science and organizational studies (Davey, 1991).

1. A specific source of inspiration in social science is constituted by the traditional study of a village or local setting in cultural anthropology

2. In political science, historical roots include a strong tradition building on case studies. Later on, when the methodology of the behavioral sciences became dominant, this tradition was partly replaced.
3. Well-known from the field of psychology are the studies of Sigmund Freud and other psychoanalysts. Later on, the study of individual persons (cases) on other domains, such as personality psychology and clinical psychology, developed.
4. More recently, the study of cases in many policy fields (e.g. social work, youth support, labor market intermediary, the integration of ethnic minorities) presents new impulses. Case study research in these fields is not seen as an admission of weakness, as it is in some domains, but as one of the central strategies for research.

In recent decades, confusion increased because the character of case studies changed rapidly within the social and the behavioral sciences. While in the past basic research, by means of a qualitative, exploratory approach, dominated the field, nowadays attention has shifted to applied research (Davey, 1991).

As in all research, in doing a case study we focus on the problem we want to solve. Whatever research project one has in mind, the research question is the point of departure. In the majority of case studies, the researcher starts with a rather broad and perhaps sometimes still vague question. If little is known about the object, one can only pose broad 'what' and 'how' questions. This does not exclude the fact that the researcher, after defining the problem, proceeds by selecting some possibly applicable theories. Generally, during the research process the broad question develops into a series of more precise questions. In most case studies, the researcher tries to maintain a maximal openness towards unknown aspects, and to 'let the object speak'. This implies – for most case studies – an exploratory approach. However, occasionally, a case study starts with precise questions, or even with a hypothesis to be tested. The latter requires an all but exploratory approach (Armisted, 1984).

In case studies, several data sources are used. Obviously, documents as well as interviews and observational data are not always available. In the eyes of many scientists, the case study

is more or less identical with field research in a natural context, as is well known from cultural anthropology. A case study, however, need not necessarily include participatory observation. The possibility to observe behavior renders the case study exclusively apt for studying contemporary phenomena. But we also use the label 'case study' for some forms of historical studies in a not too distant past. One may afterwards collect information about developments during a specified period. In historical case studies, exclusive use is made of documents (or, if the recent past is concerned, of oral history).

Particularly with respect to organizational studies, in which we want to understand an extant situation by reconstructing developmental processes through the use of documents and/or interviews with participants, but also on the macro- and micro-levels, retrospective case studies are carried out. Asking retrospective questions may give us some insight in what happened in the recent past, or about the perceptions earlier people had about each other and about the process itself. However, apart from the fact that we do not always know the proper questions to ask because of lacking information, or that we even don't know the suitable informants, answers on retrospective questions are notoriously liable to bias. If possible, collecting data 'on the spur of the moment itself' is to be preferred. Being critical about the data and the way they are gathered is one of the key requirements of the researcher's attitude (Boyce, 1993).

Injecting Realism

An important consideration when writing case studies, especially culturally specific case studies is to try to focus on real world scenarios and situations that students may encounter when they leave the classroom. Cases from real life are found to inspire students to focus on the problem solving and critical thinking aspects of the case. Unlike purely theoretical cases, real world cases often do not have a single correct solution. Therefore, the open discussion and multiple suggestions will lead students into a deeper approach to learning (Erskine et al., 2007). Lizzio et al. (2002) found that when given realistic case studies, students were far more engaged in the process, and were eager to test their problem solving skills with their peers and their instructors.

The best method for generating realistic case studies, both domestic and international, is to meet and work with actual people in real world settings. Former students are an excellent source for insight into the working environment and situations encountered by one's graduates. As a researcher, make sure you listen carefully to the situations your students speak of. There will be plenty of time later to write and format an appropriate case study later. During the interview, make sure you listen and try to understand the situations as described and understood by the interviewee. This is especially true if one is trying to understand and write about a non-familiar culture. Make sure as the author to keep in mind that how you perceive events may be very different to how the interviewee perceives them. When writing culturally specific case studies, it is important to keep the focus and the methodology on how certain events and situations will be applied and perceived by the students and not by the author.

Cultural Dimensions

The work of the Dutch scholar Geert Hofstede during his work with IBM in the late 1960 and early 1970's has developed into one of the seminal ideas for understanding and adapting to different cultures in and around the world. In his works, Hofstede identified five aspects of national culture that are widely accepted and taught to this day. These aspects are; Individualism vs. Collectivism; Power Distance; Uncertainty Avoidance; Achievement vs. Nurturing; and Long-Term vs. Short-Term Orientation (Hofstede, 1980). For an author attempting to research and identify cultural specific aspects and ideas for country specific case studies, Hofstede's work is a very good starting point.

Hofstede's first measure, Individualism vs. Collectivism, offers an indication of how an individual person would view their relative position and importance in relation to the obligations of larger groups such as co-workers, organizations at large or society in general. Essentially, in cultures high in individualism, a person would consider their wants and needs to be of more importance than the needs and obligations to the larger groups. People in high individualism cultures are more comfortable with negotiating for higher individual salaries. They would be more inclined to change positions within a company for personal

advancement, or even be willing to change to different companies for personal gain.

In contrast, individuals from cultures high in the collectivism aspect are far more likely to consider their personal needs and wants in a subordinate view of the demands of the larger corporate and social structures in which they live and work. Salaries are often lower. Transfers within the organization are more likely to be at the behest of the organization as opposed to being initiated by the individual's desires, and moving from one organization to another is far more difficult, and less acceptable (Hofstede, 1993).

Where as in the United States of America, which is high in the Individualism measure, case studies may often center around how an individual or a manager would individually address an issue or situation. Solutions are often steered towards how the individual can prepare to deal with such decisions, and often how to utilize such challenges as a way to improve their individual standing and enhance their personal career opportunities. In contrast, case studies that are to be geared towards cultures high in the Collectivism measure would be more likely to explore situations and solutions that would be more acceptable to group consensus and harmony. An understand of group dynamics, and decision making, as well as a comprehension of the desire for harmonious relationships within the group setting is essential in identifying concepts and solutions for suitable case studies.

Hofstede also identified the cultural dimension of Power Distance. In general, Power Distance is a measure of a cultures tolerance of economic and social differences between the different layers of society. In countries high in Power Distance, you may see extreme differences in the accumulation of wealth, standards of living, and even social and legal obligations and consequences between the few who are very wealthy and the many who are very poor. In contrast, countries that are low in the Power Distance measure are far more likely to make use of taxation, government programs and social programs to spread a societies riches and rewards more evenly across all layers of the social strata (Hofstede, 1993).

For the researcher, it is important to understand the different demands as well as expectations of individuals within different societies in relation to their acceptance of power distances. Such differences will obviously manifest themselves in

salary expectations, requirements and acceptance of management perquisites (executive dining rooms, company cars etc..) as well as the living standards expected of individuals in return for their efforts. In addition, Power Distance considerations often manifest themselves in the means and acceptance of professional and personal interaction between members of differing hierarchical standing within an organization. For example, in the United States of America which is relatively moderate in its Power Distance measure, it is considered acceptable for employees to have a cordial, even personal relations with your immediate supervisor. Acceptance, and even the expectation of certain aspects such as an "Open Door Policy" that both allows and encourages the casual, unplanned visitation with one's supervisor is widely accepted. In contrast, in societies high in the Power Distance measure, I would be considered unseemly for subordinates to be overly casual in their manner and tone of interaction with even their immediate supervisors. Appointments are expected, even required for all but the most pressing of emergencies, and non-work related interaction including dining with one's supervisors is unusual.

A third cultural dimension identified by Hofstede is the concept of Achievement versus nurturing. In general, cultures that are high in the Achievement orientation tend to place significant value on aspects such as assertiveness, success, competition, and performance. In contrast, cultures that place their emphasis on Nurturing tend to stress and value concepts such as quality of life, warm interpersonal relationships, service and care for the weak (Hofstede, 1993).

When researching the requirements of an individual within the workplace, it is important to know and recognize the social expectations of the employee and their place within the organization. In cultures high in the achievement orientation, workers are expected to succeed. They will be judged not only on their efforts, but also on their results. Most organizations place some emphasis on interpersonal relationships and the ability to at least deal with co-workers on a civil basis. However, the measures of success and advancement are driven in how well you perform in your assigned task, not in how well you get along with your fellow man. In contrast, cultures who measure high in the nurturing orientation place significant emphasis in the interpersonal relationship between the employee and their co-

workers, customers, suppliers etc. Although there will always be certain expectations for successful completion of assigned tasks, advancement within the organization will also require a willingness to get along and support others.

For the researcher seeking to craft case studies specific to a certain culture, it is important to know and understand the expectations, both achievement and nurturing that are expected and even required within a country or region. Resolutions to conflicts or job requirements will require a different emphasis within the differing expectations and views of the company. Achievement orientated cultures might require and expect performance driven resolutions to conflicts, and may even give preferential consideration to high achievers in matters that arise. In contrast, nurturing orientated cultures are far more likely to give consideration the external influences and personality traits when exploring conflict resolution and expectations for employees.

Hofstede also identified the cultural concept of Uncertainty Avoidance. Just as individuals differ in their willingness to take risks (couch potato vs. rock climbing) cultures also differ in their expectations and willingness to accept risk. Countries low on uncertainty avoidance tend to be more tolerant of differences between members, tend to value diversity and are generally more easy going. In contrast, countries high in uncertainty avoidance tend to value conformity to the organizational culture in which they work. They tend to be more intolerant of differences, are often ridged in their expectations and have more structured situations and working conditions (Hofstede, 1993).

Cultures low on uncertainty avoidance tend to value and reward risk takers, especially if they succeed. A great deal of tolerance is allowed to differing opinions, styles, tastes and working conditions. Not only is originality rewarded, and expected, cultures low in uncertainty avoidance tend to have high requirements and expectations for tolerance of others with differing cultural views and traditions.

In contrast, cultures high in uncertainty avoidance tend to expect a high degree of conformity to the social and cultural norms of the organization. Expectations tend to be group centered, and there is often a degree of unacceptance of differing styles, habits, and views.

For the researcher seeking to craft appropriate case studies, it is important to understand what actions are likely to be accepted and rewarded. In countries low in uncertainty avoidance, expressions of individuality are often supported and protected. Employees are often encouraged to express their differing views, and to seek out and explore new and unusual solutions to problems or opportunities. In contrast, countries high in uncertainty avoidance tend to value and require conformity to the group norms and expectations. Employees are expected and encouraged to learn the social and cultural requirements, and to adapt their behaviors, actions and emphasis to conform with the group norms. Actions and options that differ from the group expectations should be explored cautiously, slowly and with emphasis towards maintain group harmony.

The last cultural dimension identified by Hofstede is the concept of Long-term versus Short-term orientation. Cultures that are high in the long-term orientation tend to view success as a more sustainable and lasting idea. Concepts such as persistence, patience, thrift are often associated and expected within long-term focused cultures. In contrast, cultures with a more short-term orientation tend to focus on the more immediate problem and solutions. Concepts such as personal happiness, immediate success and completion of a task are often associated with a short-term cultural viewpoint.

Within cultures with a long-term orientation, problems, conflicts and solutions are viewed with an air for sustainability. Rather than seeking an immediate solution for a problem or focusing on a short-term gain, emphasis is placed on seeking and considering viable long-term solutions which are likely to be successful for many years. Expectations for organizational advancement are often lower, with an eye for eventual success at appropriate times. Conflicts and solutions are weighed with an eye for how they will affect the organization in the long run. In contrast, cultures high in the short-term orientation tend to value immediate success and solutions. Ideas and conflict resolution tends to be viewed with immediate returns and expectations. Career expectations tend to be more immediate, and sometime problematic if an individual does not feel they are advancing in proportion to their contributions.

For the researcher seeing to craft appropriate case studies, it is important to consider the different

expectations of both the individuals as well as the organizations within the culture. In long-term orientation cultures, individuals will often have expectations geared to future returns and measures of success. Likewise, organizations will often view an employee's efforts and measures of success over a longer time period. In contrast, short-term oriented cultures tend to have more immediate demands and expectations. Individuals tend to expect more immediate feedback, recognition and rewards for their efforts. Likewise, organizations tend to view the contributions of their members on a far more immediate basis. Past success or failures are often overshadowed by more recent results.

Conclusion

A case concerns a specific instance or manifestation of the phenomenon to be studied. A case study may be based on one case (a single-case study), or on several cases (a multiple-case study). Furthermore, a case may involve only one actor, such as a person, an organization or a village, or it may involve several, sometimes many, interacting actors. In addition, when seeking to craft case studies for use in non-western countries and cultures it is essential for the researcher to make some significant efforts to gain some insight and understand of the interactions within the culture. Ideally, the researcher would immerse themselves within the culture for some period of time and get to know and understand the actual interactions within the area. Meeting with managers, employees, students from and within the region is an excellent way to get some insight into their expectations, reservations and the realities of their lives. Background research is helpful to give some idea of differences that the researcher should be considering. However, being observant, listening well and experiencing the area first hand are invaluable tools to begin to understand the rich diversity and cultures of the world they seek to understand.

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CURRENT POSSIBILITIES OF THE COOPERATIVE BANKING

OTAKAR SCHLOSSBERGER

HEAD OF DEPARTMENT OF BANKING AND INSURANCE, UNIVERSITY OF FINANCE AND ADMINISTRATION,
PRAQUE, CZECH REPUBLIC

Abstract

Cooperative banks have a long lasting tradition in the Czech Republic as well as in some Central European countries. In the middle of 90's there were several ten of cooperative banks on the market.

Regulation and supervision, analogously as in the area of classic banking, were devided into Ministry of Finance and Czech National Bank.

Full paper in its first part will deal with the current position and meaning of cooperative banks in the banking sector in the Czech Republic from different points of view. As the Czech Republic is a member of the European Union, the theoretical part will deal with the exploration about so called single european license and its application for cooperative banks which is charged in Directive 2006/48/EC of the European Parliament and of the council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions.

The second part – practical part – will analyse the conditions and implementation of this license for the possibilities to impact as the cooperative bank in other state than is Home Member State on the actual case.

In conclusion the report will evaluate the called thesis with the goal to specify the possibilities and occasions of the cooperative banks in the banking sector.

Key words: cooperative banks, regulation, supervision, single european license, occasion.

Introduction

Cooperative banking has relatively long tradition in Bohemia region. The development of cooperative

banks on the territory of today's Czech Republic can be studied in 60's of 19th century. The ideas have come from Austria as in those days Bohemia region was part of Austria – Hungarian Monarchy. The plan was based on joining some financial resources in sort of treasury where the members could borrow money from. Frantisek Cyril Kampelik was the man who had the biggest credit in extending this idea. He thought that "even from small funds it is possible to collect big capital. This idea was presented in the press and public lectures of patriotic clubs and as a result the first cooperative bank was established in Vlašim in central Bohemia. The citizens joined their resources to be able to start their business. This establishment in 1859 had a big influence on further development of new cooperative banks. After several years, in 1861 there were more than 20 cooperative banks on the territory of Bohemia and Moravia, next year more than 40.

The development of cooperative banks was determined by relative self-based activities. It was the way how to obtain the funds for activities of cooperative bank. The main principle was about the fact that the necessary capital was not collected outside the bank but from inside, from own recourses, by using of personal savings and deposits of the members. This cardinal idea has been kept up to now. Some different views supposed team guarantee for borrowed money from elsewhere, but this idea has not been enforced.

The idea to create the resources for financing the wants of theirs members was so strong that there operated 153 cooperative banks on Bohemian market in 1868. These banks provided credits to small producers, merchandisers and workmen on the principal of modern business on the financial market. They used small amounts of accumulated capital which came back again on the principal of

recoverability. In these days the Czech cooperative banks were supposed to be practically the only representatives of nationally based Czech banking in Bohemian region which became the first credit source of Czech enterprisers who were of humble origin. Therefore it is logical that in further evolutionary stage the Czech cooperative banks formed the birth of majority of Czech commercial banks.

At the end of 1873 more than 520 cooperative banks worked on the territory of today's Czech Republic. Since 1873 the development of cooperative banks has been limited by the law when the direct regulation began.

It is necessary to say that on the territory of Bohemia and Moravia different types of cooperative banks have arisen. For example civil banks, business banks, agricultural banks of Raiffeisen type – better said by common name “credit unions” according to one of the first promoter of this type of banking. The progress of these credit unions was very frenetic. We can demonstrate it on the figures: In 1897 there were 600 cooperative banks and in 1912 the number increased to 3700. The first credit unions were not only volunteer and non

professional but also territorially fragmented. For that reason the influence of central institutions tended to rise. The Central association of Czech business community has been established. This institution was advisory and control subject. Even it concentrated financial abundances of some credit unions and lent them to somebody else who was in need. This institution served later as the basis of very strong bank – Agrarian bank (in 1911).

The cooperative banks were one part of banking system of the former financial market after constitution of the independent Czechoslovakia (in 1918). They had the role of the lowest link in credit and deposit system. They were called as folk credit unions which played a major role in financial business and credit system in inter-war period. They supported the effort of small savers and urban and country population and simultaneously protected their business (enterprise). On the other hand they were fragmented and their incomes were diversified into small cooperatives and only a small part of financial resources came back to the economy as the credits. At the beginning of the new state we can see four basic types of banking:

<i>Category</i>	<i>Number</i>
Savings banks	366
Civil credit unions i. e. Schulz-Delitzch type	1 413
County credit unions	172
Credit unions i. e. Raiffeisen type	3 798

The number of different types of credit unions demonstrates the compact network of these subjects.

There began radical changes in folk banking after February 1948, i. e. after changing of the economic system and starting of socialism construction. Their further development was determined more politically than economically. A new law was preparing. This law should have changed folk banking into one institution – “county savings bank and credit union”. The financial institutions of this type were established at the local authorities and their number was reduced. Before February 1948, there were 5 447 institutions, in spring 1948 of one thousand less. The establishment of the State bank of Czechoslovakia which took over some folk banking institutions and subjoined its subsidiaries

by them played a strong role in folk banking restriction. By the law from 1952 the folk banking institutions were changed into state saving banks which became specialized companies in acquiring and concentration of population's deposits [1, page 457]. By this activity they lost its origin function – to offer credit to small enterprisers. They were allowed to grant only personal credits to working people. We can say that the existence of folk banking institutions was broken for 44 years after their over than one hundred years tradition.

A new law effective since January 1996 permitted formation of new cooperative banks. The idea to boost this kind of banking was attended by a long lasting discussion about importance and position of credit unions. The main question related to the chance to compete with relatively vast network

of new commercial banks as well as to the worthless risk. After finishing of discussion, new legal modification took the basic principles of civil cooperative banks which are based on providing bank or other services only to their members. The separate law about credit and cooperative banks is in force relating to these institutions, not the law about banks. A new development of folk banking became very dynamic again. At the end of the first year of new law effectiveness there were 48 cooperative banks, next year already 71 [1, page 511]. Many cooperative banks have offered wide choice of bank products comparable with banks to their members. But turbulent expansion of this small banking segment and imperfect legal status have led to bankruptcy of lots of cooperative banks around the turn of the century or many of them have been misappropriated by their management. This situation has shown that is impossible to leave the segment of cooperative banks in general regulation and supervision only.

For that reason the law as for cooperative banks has been revised several times and the requirements concerning establishment and operation of cooperative banks have been made more strict. The year 2006 became the turning point in regulation and supervision when all subjects on financial market were merged under supervision and inspection of only one authority. This single regulation body has been the Czech national bank since 2006. Ministry of finance is the primary authority of the whole financial market. It suggests laws concerning position and activity of all financial institutions on the market including cooperative banking. Czech national bank apart from supervision and control also regulates the entry of subjects to the sector of financial market, cooperative banks as well. Czech national bank is the authority of state executive which is allowed to provide with the licence to operate as saving and credit cooperative.

This licence comes under the Single European licence in sense of respective Directive of European Union. It means, if cooperative bank asks its domestic supervision authority, it means Czech national bank for the approval to set up a business on the territory of other EU host country, it can obtain this approval if it keeps the conditions determined by the law. The conditions for obtaining such approval are almost the same as the conditions for cooperative banking. They must be fulfilled especially: the capital demands, strategic plan of development, technical and personal

facilities for this kind of business, basic internal documents focused on prevention of making legal the yields of criminal act and terrorism financing (Anti money laundering internal documents) and specified transparent cooperative organization. On the basis of submitted material the authorities of domestic and host country reach a deal when further requirements can appear especially from the point of view of host country. The requirements are presented through domestic supervision authority so that the principles of single European licence specified in directive could be observed. If the cooperative bank obtains the licence to make business as a subsidiary without separate personality on the territory of host country and this legal power comes into force, cooperative bank must inform the supervision authority of host country about this fact and on the basis of its notification the cooperative bank must ask for recording into trade register or similar list valid within the European Union.

As mentioned above, cooperative banking has long tradition in Bohemia and Moravia region. Segment of cooperative banks has been stabilized recently. Prior era of dramatic development and more dramatic collapse from the 1990s is perhaps definitely gone. According to the figures of the Czech national bank there worked 14 cooperative banks and 41 banks and foreign subsidiaries as at January 1st, 2011.

If we compare cooperative banks and commercial banks from the view of their balance sheet items level, we find out that they are incomparable. From Czech national bank material follows that the share of cooperative banks does only 0,53 % of balance sheet level of bank sector. But dynamic changes in cooperative segment expressed by the proportion of balance sheet at the 2009 year end and in next half year 2010 was 28 % and in banking sector 2,7 % only. From this indicator we can see that cooperative banking is entering into dynamic development and has its own place on the financial market.

If we want to compare other criterions which give better evidence, we could compare capital suitability and/or share of debt failures. It is evident from Czech national bank's material that share of debt failures of cooperative banks comprises 4,7 % of all debts, but the same index in banking sector comprises 5,2 %. From these index it is evident that cooperative banks are a little bit better in this index than the banks themselves. Increase

in dynamics within cooperative banks was double (1,2 % compared to 0,6 %). As far as capital suitability, cooperative sector shows an average value of 13,7 %, banks 14,97 % as at 30th June, 2010. In this criterion the banks have won but it is good to remind that the minimum value set by the Czech national bank is 8 %. It is clear that both sectors are solid from this point of view.

Both segments of financial market are supervised by the same authority, i. e. The Czech national bank and both sectors are controlled by separate legal codes.

If we compare the contents of both codes which describe the available activity of each subject, we find out that the basic products are very similar. Common people are interested in payment services, i. e. in bank deposit and payment system (domestic, international as well as cross boarding). Many clients ask for credit or loan. There are, of course, some differences in products offered but they are not apparent to everybody from the first point of view. The cooperatives are not allowed to operate on capital or money market and they are not allowed to work in the derivatives area. But these products are not so important for common users or small entrepreneurs.

The main difference between cooperative and bank sector lies in fact that the bank after obtaining a licence to make business on the territory of the Czech Republic must have the status of joint-stock Company with minimum capital of 500 mio CZK. Savings and credit union is a cooperative personality with minimum capital of 35 mio CZK. Both subjects must keep their capital in deposit of liquid money. Client of bank is mostly not related to the bank property. He is very often not a bank shareholder, while client of cooperative bank is related to the cooperative property – it is its member. The historical principles from the middle of 19th century are still valid. In order to become a client of cooperative bank, client must first become its member. He fills in an application form and put a member deposit. This way he is allowed to take part in member session and exercise his influence on the cooperative operations.

The clients are the most interested in safety of their deposits and accounts within banks and cooperatives. There we do not find any difference at all. Legally it is arranged in bank law but credit union law refers to it as well. This way the cooperative banks are classified into the same

regime of Fund deposit insurance as the banks. In this area there is no difference for clients either to save deposits in banks or cooperatives. If there was any problem, then Fund deposit insurance would pay all insured deposits. Czech national bank looks after obligation of the banks to contribute to the Fund.

However we can find the basic difference between banks and credit unions in the area of deposit products. It rests on the fact that the interests paid to the cooperators are higher as the credit unions have lower operating costs. It means that client obtains higher profit in the same credibility. If the cooperative bank is a member of CERTIS clearing system, the bank services are on the same level as in the banks in domestic system of payment. Furthermore the clients are particularly interested in the terms of system of payment, but they are granted by generally valid legal code. Neither banks nor cooperatives are allowed to „make up things“. Some differences can be found in the area of international system of payment. The cooperatives can practise such activity but hardly any really do it for the high entry cost reason relating investment into hardware and software. But there are no legal barriers.

As far as the credits they are set by the same general legal code as with the banks. But a measure of credit can be objectively limited by capital so that we could keep the regulate proceeding of maximum engagement in relation towards one client.

Credit price expressed by credit interest rate given by the cooperatives is higher but there is better and prompt service as well as personal approach to a cooperative member. If we remind the value of default credits we can say with a clear conscience that cooperative sector works very well.

Are the savings and credit unions as dignified segment on the financial market as the banks? Have they found their place on the present financial market? We can answer both questions absolutely responsibly: Yes, they have. They are under control of the Czech national bank the same way as the banks and subsidiaries of international banks, they have almost the same basic products for consumers and small entrepreneurs, their deposits are insured by the Fund deposit insurance on the same level and under the same conditions, credit accessibility is often higher and a lot of additional service is the same quality as within the

banks. According to my opinion we have not still mentioned two important points.

The first is the fact that cooperative banks have lower or even zero prices for basic services, the second point you can experience only by personal visit of the cooperative. Their staff has more time and patience and offer have better knowledge and expertise. Particularly for the reason that they must be more flexible, even though – we must admit - credit unions have more limited products range than the banks.

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[5] zákon č. 284/2009 Sb., o platebním styku (Code No 284/2009 Co., about payments)

KNOWLEDGE MANAGEMENT - A NEW ROLE OF UNIVERSITIES

HABIL ERZSÉBET NOSZKAY
BUDAPEST COLLEGE OF COMMUNICATION AND BUSINESS, HUNGARY

ANIKÓ BALOGH
SAINT STEPHEN UNIVERSITY, HUNGARY

ABSTRACT

E-learning became widespread in our era. Nowadays even the best teaching systems with excellent teaching content often underestimate themselves if they do not have at least one – minimum experimental - project for e-learning development. Moreover, the lack of available and suitable programs is not an issue anymore. The real problem is rather the choice between them. The increasing variety of different programs makes it more and more difficult to find the best-fitting one in a certain teaching system. The consequence is that a considerable part of present e-learning teaching materials fail to exceed the conventional linear way of thinking and logic, and they often use traditional old textbook-like teaching schemes as well.

In this paper we summarise our experiences gained from developing new e-learning teaching content and using them in our own teaching practice during the past more than ten years spent in higher education. The following topics and questions will be exposed:

- Where and when is it reasonable to use e-learning?*
- Can we mutually utilise experiences gained from company - and higher education-related e-learning application development; are there any best practice solutions; and if they exist, where?*
- Can e-learning be connected to knowledge management also in higher education, similarly to the company praxis, and if so, how can we connect them?*

We will also focus on the tools and possibilities of knowledge management in higher education

institutions. Finally we will observe the interlocking of knowledge management and e-learning tools and prove how these tools add value to the educational procedure.

Keywords: knowledge management, applied e-learning, tertiary education

Introduction

In our fast paced era self development and lifelong learning is imperative if one wants to keep up with professional requirements. In fact, the appreciation of the need for up-to-date knowledge pushes the issue forward. It is not only expensive but it often sets an impossible task for an individual to sit at school, that is, requiring regular visits, not to mention the fast time-barring of learning content. Each of the aforementioned factors is a different challenge for the individual, educational institutions and teachers. Even management companies and other organizations face this challenge on a daily basis.

There is a good chance to solve the problem apparently - at least partly - if we look for the solution in the IT-supported e-learning development. Although e-learning as a form of education and technology will not solve every problem, it is undoubtedly a good opportunity - combined with traditional education - to tackle the dilemmas mentioned above.

Methods

We would like to describe our experience in a Bachelor level full time program, further education in management studies and a Bachelor level economics program. In these three different areas

of training not only the e-learning curriculum content differs, but the lessons learned were also diverse due to the widely divergent nature of the study materials and educational models.

This development has been elaborated during the first full time management education program in Hungary, which is also an integral part of the first business-oriented training concept appearing in our country. The following important considerations were the basis of the conceptual background of the program:

- Our management program should be different from the traditional (information imparting) educational system not only in its title, but it must comply with the requirement that prospective managers should be prepared to solve a variety of problems arising in business life.

- Such IT supported systems should be used in the program especially in the process of problem solving, which are more attractive and enjoyable, than the conventional ones. These should also help to solve problems through active inclusion and may activate knowledge elements acquired during traditional education.

Other important features were to constructively overcome situations lacking enough information and finally reach a decision to find several sufficiently good solutions and to be able to accept it, as in real life a sufficiently good solution found in time is often worth more than the optimal but no longer current one. It is also important to find out how to combine certain data with other information in an unusual way in order to get relevant information conditions.

The goal therefore was that the e-learning modules would not aim at explicit knowledge transfer, but to support the traditional elements of education combined with problem-solving exercises.

The e-learning modules (Noszkay, 1995) should have the following three features: they should not replace either the textbook or the teacher but they should provide a practical type of training. Problem solving is assisted by the content. The latter is controlled by a search graph, which is a characteristic of classical expert systems. The graph's peaks are those strategic, tactical steps and economic calculations which are essential for acquisition. This also ensures that the learners may return to a part of a problem after the appropriate

lessons learned. Results may be stored, the learner may return to the problem, try to solve it, or simply not move forward until (s)he is happy with the result.

We would like to describe two peculiar types of teaching:

- Auxiliary solutions for the relatively few lectures within distance learning adult education.
- The so called competency trainings system for graduate adults.

Let's take a closer look at the two types of e-learning curriculum development models! The most important dilemma of e-learning courses supporting the acquisition of Bachelor degrees is, whether it makes sense to break away from the traditional linear logic of knowledge acquisition. Based on our (and other) experience it does make sense until a certain level in any case, otherwise the course may get uninteresting.

The most important features of e-learning content are the following at least in Bachelor level courses are the following:

- It is advisable to use a so called complex package (traditional textbook, workbook, video, etc).
- E-learning content is to be broken up into one-hour training unit modules.
- There should always be self assessment tests and exercises at the end of each module.

Findings

Reasonable use of e-learning can only be effective with very serious foundation and preparatory work. In addition it must not be forgotten that the quality of e-learning requires an entirely different philosophy as traditional training. The emphasis shifts from teaching to knowledge acquisition, the student becomes the main protagonist of the acquisition process, opposite to traditional teacher-centered training. Content development can only be done as a teamwork where even the teacher roles are separated (for example, some teachers prefer undertaking curriculum development, while others choose to keep in touch with the students, assist and control their progress, etc. Professional e-learning solutions may exclusively be developed and operated with such a complex set of conditions

of which only a single element is missing, the whole system is doomed to failure.

There are also other important aspects: e-learning is not a panacea, the solution to every situation, only a bonus, a technical tool to support applications where the organic integration and inclusion into the curriculum was carefully prepared and introduced. There are several forms of training, where the use of e-learning is simply inadequate as personal relationship between teacher and student is crucial, e.g. in Bachelor full time courses, where for example the importance to acquire the learning methods, value systems, certain forms of behavior, etc. having respectively at least equal importance, as the acquisition of problem solutions skills and knowledge in the strict sense.

There are such training situations where efficient operation is only possible through network-based systems like intranet and internet, for example when it is imperative to ensure the monitoring of student progress, a relatively instant student - teacher interaction, and a mechanism for consultation.

According to our judgment and experience the fundamental factor of and the key to a successful e-learning system is to clearly see and divide the educational phases built on one another during the design of its modules. These modules are indispensable for us so that we could offer a curriculum matching to the needs and preparedness of the targeted group of students, which results in the learning efficiency we had intended to reach with the invested development.

The relationship of knowledge management and e-learning

Adult training living up to contemporary expectations, that is, the realization of planned process of lifelong learning, is unimaginable without knowledge management. Companies already handle these issues together within their training plans. Pure knowledge transfer is hardly possible in business without knowledge sharing and knowledge integration. All these factors unavoidably result in new knowledge combinations, which add value on the one hand to new products, on the other hand to new, acquirable knowledge products representing a higher level of the development spiral. This knowledge integration demand should not be followed but assisted by education.

Could company and higher education e-learning developments be utilized mutually?

There is quite a lot of the experience worthy of consideration gathered on both sides. The valuable developments of e-learning companies are very impressive according to analyst observations. These developments are refined by user feedback and may well be utilized during the development of higher education e-learning systems. Unfortunately there is no or hardly any dialogue on this issue between the two stakeholders in all these areas. Even among higher education institutions in this area the merits of cooperation e.g. joint developments or the transfer of learning content itself, do not exist. This is a serious problem as really good e-learning curriculum development is very labour intensive. So if the institution intends to produce a development beyond textbook adaptation, based on the linear logic of thinking patterns, they must face the fact that they could get results from only the best team, a group of teachers and experts, whose commitment and interest is vital. It is not simple, since the majority of teachers are not really motivated to change. To unlearn the old and traditional educational methods (lecture - textbook - traditional assessment methods) requires an entirely new approach. It can clearly be seen that not everyone is capable to this shift, concerning the development of e-learning materials in particular.

Universities as knowledge bases

The following factors mentioned below make the knowledge base role of universities and higher educational institutions and their increased responsibility a current issue.

According to Wissema (Wissema, 2009) the third generation university in the 21st century's knowledge-based society augments knowledge production; the capital profile of higher educational institutions is the most significant sector. While the production of knowledge broadens out at the same time maintaining a strong connection with its traditional production places, the actual field of use and opportunities turns into direct practice.

The demand of lifelong learning is attached to the former phenomenon, which means success and career on the long run for the individual, while for the organization it is the basic condition

for knowledge production (Noszkay, 2008). This means a practice oriented enlargement of the education palette, which also uses information technology and distance learning methods. At the same time a novel use of university knowledge not only adds value to the cooperation with business partners, but the results could enhance university education, integrating contemporary knowledge. This has an outstanding significance, because in information society knowledge quickly goes out of date, therefore the permanent refreshment of university knowledge bases, likewise the continuous training of the individuals keeping pace with the latest results, is a fundamental issue to be tackled within the whole society.

As a result of the cooperation with strategic partners content development of Bachelor level education could come closer to the real demands of the labour market. Such tutoring systems should be built, which serve students' problem solving competencies and skill development. Competency based adult training programs, e-learning systems in distance education, within the frameworks of lifelong learning, adapted to learner needs could be initialized with better foundation opportunities, in cooperation with the region's business sphere, consultancy organizations, chambers and professional alliances. The opportunities of university education and knowledge management systems can be broadened with the most up-to-date technologies, solutions and IT tools.

All the above mentioned issues points towards the fact that the university tends to cooperate with the market and other players on a higher, closer level in the fields of society and the region, especially on the area of knowledge integration, management of knowledge basis and knowledge sharing.

Knowledge distribution matched with the demands of lifelong learning has an outstanding role in this process, which offers a new role to traditional universities. These cooperation networks of university innovation centres and companies, knowledge creation and knowledge sharing with the support of e-learning systems has a fundamental significance.

Knowledge application in higher education institutions – the use of e-learning and blended learning tools

We would like to focus on knowledge application as the most important factor of knowledge management. Institutions should store information in user friendly, searchable systems so that stakeholders (students, teachers, administrators) have easy access to it.

Traditionally knowledge transfer towards students is realized in person by the teacher or by books, notes. In the past 10 years higher education institutions (HEIs) gradually introduced different online media to utilize various possibilities of the internet. These tools cover two main fields: administration management and content management. These systems are used by all stakeholders on an everyday basis within the universities and colleges.

Education Administration Systems

Electronic education administration systems take over the traditionally offline student administration thus students may manage their own activities online (e.g. applying for exams, being informed about their grades, etc.). The administration is not 100% automatic though, administrators still manage most of the student activities, but it is more transparent for both parties to have a searchable and accessible online overview of student matters. These systems fulfil the requirements of an electronic knowledge management system described by Maier: „ a KMS (knowledge management system) is a technological part of a knowledge management initiative that also comprises person-oriented and organizational instruments targeted at improving the productivity of knowledge work.” (Maier, 2005). As in most countries it is obligatory by law to use such a system, we can say that there is a knowledge management system in all university and college.

Learning Content Management Systems

According to the definition of OECD Learning Content management Systems are „... software designed to provide a range of administrative and pedagogic services (related to formal education settings (e.g. enrolment data, access to electronic

course materials, faculty/student interaction, assessment, etc.)". (OECD, 2005)

In the past years it has been proven that the so called blended learning is the most suitable for student needs (Garrison, Vaughan, 2008). Students consult the teacher during lectures and seminars and they receive learning material online. They also keep contact with each other and the teachers on online forums. The effectiveness of this new type of communication is ensured by quality management procedures and documentation. The blending of online and offline elements depends on the type of education. In full time education the learning management system (LMS) offers background services while part time or distance education is organically built on the services of LMS.

Problems and solutions

As institutions usually apply other information systems like Enterprise Resource Planning Systems (ERPs), Management Information Systems (MISs) or an Intranet portal with Web 2.0 functions the question arises whether there is a risk of redundancy and defragmentation of knowledge. Why is it necessary to use all these kinds of systems? The answer lies in different functionality.

The LMS offers educational content, the Education Administration System assists administration (timetable, exams, etc.). These different types of systems complement each other and are retrieving data from the same databases, e.g. curricula, student personal data. Using a single sign on (SSO) authentication would ensure a more user friendly approach and interface. The use of SSO is not wide spread yet though in tertiary education. There is a possibility though of building connections between the different systems. System administrators and developers work as a team continuously searching for better solutions thus assuring a synergy.

The rapid proliferation of mobile tools and the use of Web 2.0 possibilities like Facebook, Twitter, Flickr, wikis, webinars, etc. also offer tremendous opportunities integrated into and outside the LMSs.

Conclusions

The main goal of knowledge management is enhancing organizational effectiveness. Though higher education institutions and companies differ in most aspects, in this case they would like to reach this same objective. Similar situations occur in both types of organizations e.g. employees leave due to changing their workplace or superannuation. In these cases it is imperative to store and transfer the employee's knowledge so that it would not be lost for the organization.

Universities and colleges are in a unique situation: they not only manage but also create knowledge. All participants of the knowledge creation and transfer (students, teachers, administrators) benefit from the use of knowledge management systems described above.

Students use Web 2.0 features of the new media to individually managing their studies, communicating with their peers and teachers online, accessing knowledge whenever and wherever they need. Thus they gain new competencies like the ability to study individually, better self-management capabilities, more self confidence.

Teachers need to further develop their IT skills to keep pace with their generation Y, or Z students who are born into the digital world. Also LMSs offer the possibility to record and store their knowledge online e.g. as Frequently Asked Questions on an online forums, as a consequence there is no need to answer each student question one by one. So the use of online media ensures more teacher time and energy. Administrators can track and trace back student issues easily with the help of Education Administration Systems.

In this procedure e-learning and blended learning is not a panacea but an opportunity to ensure effectiveness.

Implications

As a summary let's devote some thoughts to the not-too-distant future. We think in further adult education integration of knowledge management is inevitable. Note that knowledge management and e-learning is already in symbiosis within the training systems of companies. In business sector it is difficult to image only knowledge transfer without knowledge sharing and integration. All of this will inevitably lead to new knowledge combinations,

which in the service of value creation will result in new products and new "knowledge products" which is on the higher level of the development spiral.

Education should not only follow but facilitate this need for knowledge integration.

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MANAGERIAL PERCEPTION OF COMPETITION: EVIDENCE FROM POLAND

MAGDALENA KRZYŻANOWSKA
KOZMINSKI UNIVERSITY

MARIAN MOSZORO
IESE BUSINESS SCHOOL & UNIVERSITY OF CALIFORNIA, BERKELEY

Abstract

Understanding competitors' decisions is essential for businesses in competitive markets. However, managerial perception of competition has been largely neglected in the management literature and totally ignored as it relates to transition economies. Based on qualitative data from in-depth interviews, we explore how senior-level marketing managers in Poland perceive and respond to competition. We find that decision makers accurately identify competitors but give little attention to competitors' activities that may affect their own performance. Results suggest that there are areas in which companies can undertake marketing initiatives without risking competitors' immediate market reaction.

JEL Classification: D81, D83, D84, M21, M31

Keywords: Competitive Analysis, Managerial Perception, Cognitive Biases, Strategic Management, Marketing

Introduction and objectives

Competitive analysis is essential in formulating effective marketing strategy (Kotler et al. 2009). An in-depth analysis of competition is beneficial and increases the likelihood that the company can achieve its goals (Curren et al. 1992). However, competitive analysis is not easily employed in practice, as it involves the complex tasks of obtaining, processing, and interpreting large quantities of information. Not all managers go about this task in the same way, so the perception of competitors' activity is subjective, and it shapes marketing decisions subjectively (Barnes 1998, Greve 1998, Maule & Hodgkinson 2003). Therefore,

managerial perception of competition has emerged as a distinct field of research (Thomas & Pollock 1999).

Although much has been done to improve our understanding of how managers identify and perceive their competitors and how their interpretation of competitors' behaviour influences the decisions they make, most studies have been carried out in Western countries (e.g., the US and Great Britain), whose economies have always been market-oriented. Research has not been conducted in countries that have undergone political transformation, and in which, consequently, market mechanisms—including competition—have developed rapidly, rather than over a long period. Because competition has developed in diverse ways in different economies, the lack of knowledge about perception of competition in transition markets is a gap that should be bridged. The purpose of this article is twofold: (1) to examine perceptions of competition held by marketing decision-makers in transition economies and (2) assuming that managerial perception of competition influences decision-making, to investigate the marketing implications of managerial representations of competition in these economies.

The paper is based on qualitative research conducted on the Polish market among senior-level marketing managers. The Polish market belongs to the group of countries that have undergone the political transformation that commenced in 1989.

The paper consists of four sections. We begin by highlighting the literature on managers' perceptions of competition and their influence on decision-making, especially on marketing decisions. Next, we describe the study's methodology and explain the reasons for the choice of qualitative research.

Section 3 contains the results and conclusions, and we close by describing the study's limitations and suggesting topics for further research that stem from our analysis.

1. Literature review

How managers analyse their companies' competition has been a topic of interest for many years. This research stream concentrates on the issue of developing mental representations of competition to be shared and used by executives to evaluate their environment, to identify their rivals, and to define the dimensions along which they compete. The trend toward competitive analysis was present in research earlier, but it began to develop fully in the 1990s as a response to the structure-conduct-performance paradigm (S-C-P) and the subsequent strategic groups concept, which was based on the assumption that the economic characteristics of firms in an industry explain the dynamics of rivalry in that industry (Thomas & Pollock 1999). This stream of thought was inspired by the theory of bounded rationality (Simon 1972, Williamson 1979), which suggests that individuals are limited by their information-processing capacities.

Within the framework of this theory, are two primary research problems connected with managers' perceptions of competition: (1) the essence of the process and (2) the diversity of managers' perceptions. The study of the essence of the managers' competitor-perception process, which is intertwined with the study of the managers' cognitive processes, has established that, when identifying competitors, managers use simplified models to which they apply self-created cognitive categories based on the similarities and differences they detect between subjects. With these cognitive models, they develop a simplified view of the complex competitor structure (Porac & Thomas 1990, Clark & Montgomery 1999). As to the second research problem, the variation in the perception of competition processes, research has determined that the subjective perceptions of managers can result in seeing competitor conditions differently (de Chernatony et al. 1993a, Daniels et al. 1994, Hodgkinson & Johnson 1994, Daniels et al. 2002), a framework that also involves the notion of representation durability. That is, managers may become attached to their interpretations and cling to them despite new developments in their environment (Reger & Palmer 1996). Some

studies have addressed the influence of various perceptions on managers' ability to identify the type of competitive advantage (Day & Nedungadi 1994), as well as the similarities between the company's perception of competition and that of the consumer (de Chernatony et al. 1993b).

The key conclusions that can be derived from these studies are that (1) managers are dedicated to competition analysis to varied degrees and (2) top managers can make mistakes in assessing their companies' competitors. The degree of managers' dedication to competitor analysis varies between those who simply describe the current situation (e.g., their competitors' aims, advantages, and adopted strategy) to those who also attempt to predict their competitors' moves or even try to predict their competitors' reactions to the company's activity (Montgomery et al. 2005).

Errors in competitor analysis may be the consequence of lack of emphasis or overemphasis on competition (Leeflang & Wittink 1996). When the emphasis is too spare, four phenomena often result: (1) the 'winner's curse,' that is, insufficient consideration of the contingent decisions of competitors, which leads to mistakes in judgement, (2) irrational escalation of commitment to projects, (3) overconfidence in judgement, and (4) limited perspective and problem framing (Zajac & Bazerman 1991 in Deshpande & Gatignon 1994). When the emphasis is excessive, too much focus on competition can hamper creative problem solving and distract managers from thinking about other important goals (Deshpande & Gatignon 1994).

Our study contributes to the efforts to understand perception of competitors and to identify its consequences for managerial decision-making by considering the convergent points of competitor perception and marketing decisions.

2. Research approach and methodology

For the purposes of this study, a senior-level marketing manager is the unit of analysis. Since we adopted the inductive approach, inspired by grounded theory, we initially assumed the sample would grow as the study developed and factually justified postulates appeared (Cresswell 1998, Konecki 2000). However, limited access to top managers forced us to adopt the simplified

method of predetermining our respondents in order to adhere to the maximization difference principle of diversity between studied phenomena in explorative studies (Denzin & Lincoln 1994). We adopted several criteria in choosing subjects of our study so there was a reasonable distribution among: (1) type of buyer (consumer/business), (2) type of activity (production/services), (3) company size (large/medium), (4) industry, and (5) market stage (growing or mature). In addition, the subject's company had to (6) have a marketing department (a technical criterion to help recruit respondents) and (7) be characterized by relative independence in decision-making (e.g., representatives of foreign companies were excluded).

The qualitative data collected during the study were taken from the comments of marketing managers from the selected companies. We gathered data by means of in-depth interviews based on a scenario involving three thematic blocks with three questions each. The questions concerned three issues: (1) the information about competitors the managers consider necessary to make a decision, (2) the types of decisions made by marketing managers, (3) who is considered a competitor and which competitor behaviours are analysed. The extended questionnaire and coding sheet are provided in the Annex.

To avoid exposing the main area of interest of our research and possibly biasing responses, we announced our topic of interest as tools for development of managerial skills. Focusing the respondent's attention on a hypothetical market and managerial situation allowed us to minimize the respondent's discomfort in disclosing information about actual competitors and to control for hiding or exaggeration effects. The introduction to the interview explained the general idea of using the company as a case study for managerial skills development, and the respondent took the role of practitioner-expert. Questions were broad in order to encourage open responses. The role of the interviewer was to ask clarifying questions once respondents' spontaneous responses were exhausted.

Thirteen interviews were carried out in October and November 2008. The respondents were employees of medium and large companies operating in Warsaw, Poland. Interview times ranged from 45 to 60 minutes. All interviews were recorded with the subjects' consent, and afterwards faithfully transcribed. Data analysis was carried

out by means of matrices based on coding sheets. The analysis, which was of comparative character, served as the basis for drawing conclusions and constructing general categories (Miles & Huberman 2000).

3. Findings and conclusions

The outcomes of this research can be divided into two threads: competition characteristics from the point of view of the company's decision-makers and the role of competition processes as the motive behind marketing decisions.

In order to comprehend managerial perceptions of competitor activity, it is necessary to determine how decision-makers define competitors. Respondents usually mentioned one to three criteria. Apart from classic criteria, such as similar products, the same target group, similar resources, and company size, respondents listed flexibility, dynamic development, better offers for buyers at a given time, and company location.

The respondents predominantly defined their competitors as companies that offer a similar product, that target the same buyers, and that generally resemble the respondent's company. A few managers identified dynamically developing market members as a threat, but many interviewees failed to refer to emerging companies. Therefore, there may be two ways of perceiving competitors: the short-term perspective and the long-term perspective. The short-term perspective is characteristic of market agents who focus on the present, while the long-term perspective is characteristic of those who try to predict future outcomes and to foresee future threats by analysing currently insignificant but dynamically developing entities. Interviewees rarely mentioned the substitutes criterion, and one of the managers even declared, 'We do not perceive them as ... such a big threat.... We don't go that far.' Most respondents saw their lists of the criteria they used to define competitors as rather simple and, irrespective of the number of criteria they provided, enumerated them easily. This level of ease and familiarity suggests that managers employ a certain routine and refer to the schemas they use on an everyday basis.

The respondents can also be split into two groups depending on the level of difficulty they ascribed to the task of identifying a competitor. Respondents who included among their competitors companies that offer substitute products and respondents in the B2B sector found the task of defining competitors far more demanding than others did. These respondents argued that the task was difficult because of the market's transparency level and because the difficulty in identifying competitors notably increases with a rise in substitute products. Respondents in the B2B sector emphasized that personal contacts with clients make it more difficult to identify competitors at an early stage.

The results of the study lead to several significant conclusions. First, most respondents have a reasonably well grounded and stable approach to defining who their competitors are. However, because respondents use various combinations of criteria, their perceptions of competitor activity differ, so managers of objectively competing companies do not always subjectively identify all of their competitors, even though their competitors identify them as their rivals. As a result, these managers often overestimate or underestimate their competition in the process of delineating the company's strategy, which can influence the efficiency of marketing activities. When the competition is overestimated, the company impairs its efficiency by refraining from steps that might provoke its competitors, while a company that underestimates its competition may unwittingly activate its competitors and fail to perceive some competitor actions as consequences of its own activity. Overall, the respondents pay more attention to competitor actions than their reactions, suggesting that engaging in competitor processes is associated with adapting to current competitor processes more than with shaping them.

When identifying their competitors' activities, respondents focused on promotions, especially advertising and media presence; pricing policy; new product launches; and, to a lesser extent, competitors' investments. Other competitors' activities rarely mentioned related to distribution, services (e.g., training for clients and intermediaries), enhancements and upgrades of old products, trademark awareness, and public relations. This disproportion in the weight ascribed to different competitors' activities can be the result of specific conditions in which the respondents' companies operate, such as few competitor

activities in certain areas, resulting in little need to observe those types of activities. However, disproportion in the kinds of competitors' activities the respondents scrutinize can also lead to a fragmentary, rather than accurate, perception of competition. Therefore, if some activities receive relatively less attention from competitors, then there are areas in which companies can undertake activities more freely, without running the risk of evoking their competitors' immediate reaction.

Some respondents mentioned sales volume and market share (sometimes also place in rankings) as key indicators of competitors. This approach allows direct comparison with competitors, which is possible when those indexes are available, but it also shows a tendency to oversimplify the process of analysing competitors' behaviour, as those indexes reveal only certain aspects of competitors' activities.

Some respondents spontaneously cited the need to overtake competitors, to 'be the first, in introducing a new product, service, or delivery system (pioneers, leaders). There were also respondents who had the opposite motivation and preferred to copy solutions undertaken by competitors after the competitors had borne the cost of developing them and proving their value (followers). Still other respondents said that they observed competitors with the purpose of avoiding direct confrontation with them, that is, to 'cool off' their level of competition (niche activists). The different motivations correspond to classic marketing strategies: pioneer, leader, follower, and niche activist.

One of the respondents stated that observing competitors is useful in foreseeing possible revenge actions, that is, actions that neutralize a company's marketing activity. None of the other respondents referred to this issue in any way, which suggests that they are primarily concentrated on observing their competitors' actions, not their reactions.

Another thread that appeared in the responses about observing competitors was the different weights that managers put on time horizon. For one of the respondents, observation of competitors was important only in the short term: 'Competition is not something on which we build our long-term strategy. We have our vision, our strategy. We build it based on other stimuli.' The same respondent also said that observing competitors is useful in the context of actions undertaken ad

hoc in response to competitors' actions, but that these actions should not be a benchmark for the company's long-term planning.

At the beginning of our research on the influence of competition on marketing decisions, we considered how we could discover this influence relying only on managers' responses. Since we wanted to avoid asking directly about which marketing decisions are made under the influence of competition analysis (we feared disguised responses from straightforward questions), we asked about which decisions are the most important, what information needs they have, and how they assess access to information about competitors. This sequence of questions allowed us to rank marketing decisions among managerial decisions and information about competitors among all information.

All respondents underscored that their managerial responsibilities were not only related to 'marketing,' as their formal position names suggested, but that they were involved in general management decisions as well. Respondents mentioned that personnel decisions were the most important and most difficult decisions.

After personnel decisions, respondents mentioned financial decisions and their role in allocating budgeted funds to marketing activities as important and difficult. As especially important marketing decisions, they cited the choice of advertising media, message, and promotion. Among other decisions, they mentioned ways of motivating salespeople, including defining sales targets. Some respondents acknowledged difficulties in choosing suppliers and contractors, consulting firms, and intermediaries.

Respondents presented several types of decisions closely related to marketing strategy as important, particularly the introduction of a new product, price policy, and the search for new markets.

When asked about the information they need to make the decisions they had mentioned, respondents were not always able to distinguish between types of information and where this information comes from. Therefore, some respondents cited names of studies or reports and informal sources of information, such as clients, partners, and former competitors' employees.

Abstracting from their inability to differentiate sources and types of information, respondents

remarked that they pay particular attention to monitoring competitors' sales volume and market position, the effectiveness of their marketing actions, advertising activities (with an emphasis on their presence in media and the content of their communications), and plans for the introduction of new products. However, the information about competitors that they said they needed most was related to advertising activities and the introduction of new products, so not all of the competitors' marketing-mix elements are equally analyzed.

Respondents' answers indicate that the respondents are disinclined to do detailed competitor analysis and, in contradiction, that such analysis is indispensable. This contradiction may be a result of distrusting research results and available information about competitors, as some interviewees argued that the research done by consulting companies was worthless, that most of the reports available were 'canards', and that certain types of activity (B2B, specialist industries, non-listed companies) made it impossible to collect and access valuable data.

Respondents who had resigned from attempts to do in-depth analyses of their competitors pointed to what were, in their opinion, immovable obstacles to information access. However, others mentioned the willingness to learn from their mistakes, such as focusing more on identifying threats from new market players. The main areas of competitor analysis they pointed to were marketing communication, especially as it pertains to advertising, but also advertising budgets and the organization of the company's internal processes.

4. Limitations and further research

The key limitation of this study results from the character of qualitative research and the number of interviews conducted, both of which limit the ability to draw general conclusions. Still, we believe that diversifying the respondents facilitated our ability to identify problems connected with the perceptions of competitors by managers active in the Polish market. The qualitative character of the study made it possible to identify new research goals, the achievement of which will require a larger representative sample. Further research will involve answering to the following questions:

(1) Why do competitor identification, the level of difficulty ascribed to identifying competitors,

and the types of analyses applied to competition analysis vary from company to company?

(2) On what is the choice of competitor identification criteria dependent?

(3) To what extent do companies try to predict the marketing actions and reactions of competitors and on what is this degree dependent?

(4) What competitor activities can pose a serious threat to the company are not closely monitored and why?

(5) Which companies are most strongly shaped by limited competition analysis in their marketing and why?

The use of quantitative methods in future research will further our understanding of how managers in transforming economies perceive competition and use those perceptions to make marketing decisions.

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Annex – Extended questionnaire and code sheet

Guidelines for recruiters

Respondents are informed that the object of the research is to prepare tools for development of managerial skills.

Script for interviewers

The interviewer explains the topic of the research more extensively than it was done at the recruiting stage. The primary aim of this introduction is to avoid fears of extraction of confidential information and to foster the respondent's openness. The interviewer assures the respondent that he or she will not be asked about confidential information and that what is important is his or her general experience as a manager, regardless of position at a particular company.

Introduction

The aim of our research is to develop teaching tools to enhance managers' decision-making skills. One of these teaching tools for managers is the case study, that is, materials based on real market situations. Commonly, case studies deal with a particular company at a particular moment. When preparing a case study, the case-writer tries to reflect faithfully how managers perceive reality. I would like to ask you what, in your opinion, a case should contain in order to reflect managerial situations like decision dilemmas accurately.

1. What kinds of decisions do managers take? At your position, what are the most important and

most difficult decisions you make? (If the answer is too general, inquire at least about categories. Exclude personnel decisions.)

2. What kinds of information do managers need in order to make important and difficult decisions? What sort of information is the most important? Why? If you had only a little time to run your company (because you have other duties or because you like playing tennis), what information would you ask for and in which order? (If necessary, ask to rank information about competitors in decisions regarding actions to be taken by the company. What does this information contain? What ratios are used?)

(Pitch to Question 3) A case study is like a second medical opinion. Especially when they deal with complicated cases, physicians consult colleagues, sending them reports along with the clinical history of the patient, the results of analyses, and so on. The physician who is giving the second opinion cannot check the patient directly, so his or her opinion and conclusions are based on the information submitted by the first physician. Case studies work similarly in that they are based on the information prepared by the case-writer, and the reader formulates his or her conclusions and proposes decisions to be made, along with the possible consequences of these decisions.

3. What information should a case contain about external current market conditions? What areas should it cover? What is important for decision-making about the functioning of the company? What is the minimum information that the case should contain? What are the limitations in accessing this information? (Instruction for the interviewer: underscore that it a case is not necessarily about the ideal situation!)

4. What information about competitors should the case contain? (Ask this question if the answer did not appear in Q3. Eventually, link back to the introduction to Q3. Hint: What information about the patient's environment should be submitted for a second medical opinion?) In general, what criteria should a company fulfil to be treated as competitor? (Hint for the interviewer – possible criteria: competition closeness, e.g., direct/indirect/potential; size; successes; offensive/revenge activities; similar resources/skills; similar satisfied needs.)

5. Have you seen any useful models/approaches to market analysis? Any that are useless? What are they? (Ask further about models for competition analysis.) Which model/approach to competition analysis do you use?

6. (Hint: Let's compare competition analysis to radar.) For what kind of decisions is the information about competitive threats relevant (i.e., for what kinds of decisions do you look at your radar)? In which kind of decisions do you compare your company to your competitors? (Inquire about the importance of information about competition threats for marketing decisions if the answer did not appear spontaneously, e.g., when introducing a new product, setting price, organizing distribution or terms of cooperation with intermediaries, highlighting or promoting a product, setting the promotion budget?)

7. Are there decisions for which information about competitors is irrelevant? Which ones and why? Is there any information about competitors that is supplied to managers needlessly? (Hint: if you got stacks of papers about your competitors, which one would you just read and which would you not read?)

8. Let's forget about your current professional situation for a while and think about different sectors and companies. Do companies differ in terms of their information needs about competitors? (If 'no,' ask why not. If 'yes,' ask what it depends on, e.g., the company's size, market position, sector, speed of market development, managers' experience, type of strategy, others?)

9. If you could legally get any information about your competitors that is difficult to get, what would it be? Why?

EXPLORING THE SUPPLY CHAIN ORIENTATION: THE CASE OF CROATIAN MANUFACTURING COMPANIES

DARIO MIOČEVIĆ
UNIVERSITY OF SPLIT, CROATIA

GORAN DEDIĆ
UNIVERSITY OF SPLIT, CROATIA

Abstract

Supply chain orientation is defined as the extent to which there is a recognition among chain members towards viewing the supply chain as an integrated market entity. Previous research efforts have confirmed that supply chain orientation is a necessary prerequisite for the successful management of upstream and downstream flows in supply chain. The goal of this paper is to investigate the nature of supply chain orientation within a production firm context. In order to reveal its role, the supply chain orientation was related to the organizational buying effectiveness. Data was obtained through the questionnaire and analyzed using PLS modeling on the sample of 123 middle and large-sized Croatian manufacturing companies. Findings suggest that supply chain orientation is positively, directly, and significantly related to the organizational buying effectiveness. Furthermore, the implications of this study confirm the plausibility of viewing the supply chain orientation as a vital organizational capability. Finally, theoretical and practical implications are presented, as well as limitations and suggestions for further research within the field.

Keywords: supply chain orientation, organizational buying effectiveness, organizational capability, manufacturing industry

INTRODUCTION

Supply chain can be defined as a set of organizations directly and indirectly involved in the value creation process for ultimate customer. Value creation processes are both downstream

and upstream, involving direct and indirect flows of products, services, finances and information. Supply chain can be viewed as a system of organizations that have a goal of developing the value proposition for customers. At the same time, supply chains are oriented towards supply and demand side. However, sometimes organizations are focused only on one side of the chain which eventually results in a myopic behaviour. So, for an integrated supply chain, organization must have focus both on the upstream and the downstream side of the chain.

Supply chain success depends on the ability to integrate diverse goals and strategies of its members. Integrative efforts can be achieved through the relationship development with the members of supply chain. In their recent article, Mentzer, Stank and Esper (2008) suggest that contemporary firm has a goal to integrate all external relationships it has with its business partners. However, it must be noted that not all relationships should be treated equal. The importance of relationship is equal to the amount of value each partner provides (supplier) and for how much value added revenue it is responsible (customer). Thus it is justified to valorize both the supplier's and customer's efforts in the value creation for ultimate consumer. This advent has been defined as a supply chain orientation (SCO) (Mentzer et al., 2001). SCO endorses the idea that value creation is a process in which all members of the chain must invest their resources, capabilities and know-how. Earlier research has provided evidence that firms which have a SCO leverage higher performance outcomes (Min and Mentzer, 2004; Min, Mentzer and Ladd, 2007; Hult et al., 2008). However, the research goal of this study

is to explore SCO's influence on the purchasing performance outcomes. For the purposes of this study, the purchasing performance is measured with the dimensions of organizational buying effectiveness (OBE). The main role of effective purchasing is to act as a value creation mechanism in the supply chain.

Having in mind the goal of this study, the paper is organized as follows: First, the theoretical background of supply chain orientation is investigated. It is followed by the conceptual development. Furthermore, methodological aspects are proposed along with the operational definitions and analytical issues. Methodology section is followed by the results regarding the measurement properties and structural model. The discussion of research results is strengthened by the theoretical implications of study findings. Eventually, the conclusion, comprising the managerial implications and suggestions for further research, is presented.

SUPPLY CHAIN ORIENTATION – THEORETICAL BACKGROUND

Mentzer et al. (2001) warned that it's crucial to separate the supply chain structure from the phenomenology of its management. Supply chains exist no matter the management efforts. Inter-organizational relationships are drivers of SCM in which every member must endorse other members' efforts in the value creation process for customer (Lambert, Cooper and Pagh, 1998).

The interrelation between upstream and downstream flows within supply chains necessarily leads to the appearance of supply chain orientation (SCO). SCO endorses the importance of viewing both the customers and the suppliers as strategic partners in the value deliverance process for the ultimate customer. Mentzer et al. (2001, p. 14) defined SCO as a "recognition by a company of systematic, strategic implications of the activities and processes involved in managing the various flows in supply chain". A systems perspective is essential to clearly specify the scope of SCO. As a system, organization interacts with the other sub-systems (suppliers and customers), and they altogether comprise one larger system (the supply chain organization, in this case). Mentzer et al. (2001) indicate that firms engaged in supply chains should be oriented towards a cooperative effort aiming to enhance SCO. Taking

into consideration the importance of supplier and customer relationships in SCM, Alderson and Martin's (1965) transvectional approach provides the conceptual background for SCO. Transvections are viewed as ongoing transactions between the partners in a supply chain. The focus is on an ongoing collaboration, about which Alderson and Martin (1965) state that using the partners in a channel setting makes the channel optimal and more value is thus transferred. Reinartz, Krafft and Hoyer (2004) argue that a relationship can not be viewed as a single transaction, but rather that it has a dynamic perspective which confirms the transvectional nature as well.

SCO can also be considered as an organizational capability which aims to recognize the systemic and strategic implications of operative activities enrolled in managing various value flows in the supply chain (Mentzer et al, 2001) Hult et al (2008) offer rather different perspective stating that SCO is a multidimensional concept comprising: customer, competitor, supplier, operations, logistics and value chain orientation. The main critique of this approach comes from the close dependence with functional aspects of organization. The differences between these two approaches can be found in theoretical traditions. Mentzer et al (2001) conceptualize SCO as a behavioural phenomenon, whereas Hult's et al (2008) conceptualization considers SCO to be a dimension of organizational culture. Nevertheless, as an integration mechanism, SCO facilitates balance between the supply and customer oriented processes by implying their equal importance in the value creation process for customer. To gain benefits of SCO, organization must develop a belief that each member of supply chain adds value with its business processes and activities.

The nuisance of integrating key business processes within firm was an agenda of earlier research efforts within SCM (Ellram and Cooper, 1990, Cooper and Ellram, 1993) Therefore, SCO is meant to thrive from relational philosophy which supports the integration of inter-organizational processes in the value creation for ultimate customer. In their study, Mentzer and Min (2007) conceptualized a robust structural model where they confirmed that SCO mediates the link between market orientation and firm performance. Simultaneous orientation, both on the supplier and customer side, leverages the firm performance, because value for customer is not solely result of fruitful relationships with customers, but also with suppliers. SCO as an initiative is based on the relational antecedents

who are shown to be important managerial components in supply chains (Lambert, Cooper and Pagh, 1998)

SCO is an ideology of a single firm. It is created, developed and maintained within the single firm. But repercussions of SCO are exceeding the single firm boundaries. If the firm focuses only on one side of the chain (upstream or downstream) the SCO will vanish and the value creation process will fail at some point. Min and Mentzer (2000) define SCO as a multidimensional concept which is characterized by several activities:

- 1) Systemic approach in viewing the marketing channel as a uniform entity.
- 2) Managing the total flow of products, services and information from first-tier supplier to ultimate customer.
- 3) Cooperative efforts in order to synchronize and align operative and strategic capabilities in a unique resource unit.
- 4) Orientation on customer needs with the goal of creating customized value propositions.

Development and implementation of SCO within a single firm is influenced by relational dimensions which are derived from relationship initiatives with partners in the supply chain. Relationships within supply chains are nurtured by the existence of relational factors. According to Mentzer et al (2001), the most important relational dimensions that explain SCO are: trust, commitment, organizational compatibility, cooperative norms and top management support. It is evident that relational variables are vital antecedents in the implementation of SCO. In this way it is justified to identify these dimensions as a theoretical platform which defines the relational nature of supply chain relationships. Besides relational dimensions, SCO comprises the component of top management support. The top management support is much needed when organization tries to implement new initiatives and ideas. As a systemic mindset, SCO is under a great influence from relational factors which in the end stress the importance of other members in the value creation process.

Esper, Defee and Mentzer (2010) undertook an exhaustive literature review to identify the previous definitions and conceptualizations of SCO. Their findings indicate that SCO cannot be understood without incorporating both a firm's strategic

intention to compete via supply chain capabilities and the firm's internal structural elements. To sum up, the organization which has implemented SCO should embrace relational factors originating from relationships with partners in supply chain. In such manner, relational factors are becoming latent capabilities within a supply chain organization. Hult et al (2008) stressed that SCO should be assessed as a strategic organizational capability. Besides the key organizational processes (SRM and CRM), SCO creates a mindset which acknowledges the importance of other members in the value creation process for customers.

CONCEPTUAL DEVELOPMENT

Very little research has been undertaken surrounding the concept of SCO. However, early market orientation literature can serve as a benchmark in developing the conceptual model. The link between market orientation and business performance has been widely researched relationship in the marketing literature. Most of these studies confirmed that there is a positive, direct and significant relationship between these two constructs (Narver and Slater 1990; Jaworski and Kohli 1993; Ruekert 1992; Deshpandé and Farley 1999) Following the recent theoretical achievements in the area of supply chain management, it can be concluded that marketing has a great influence over the development of this discipline (Parente et al., 2008). Mentzer and Min (2004) developed a model in which they found positive and significant relationship between SCO and business performance. Min, Mentzer and Ladd (2007) have identified and empirically verified that market orientation should be valorized as the part of supply chain orientation. Hult et al. (2008) offer a model which explains the SCO's positive and significant influence on the firm performance measured by balance scorecard. Contrary to Min and Mentzer's approach, Hult et al (2008) viewed SCO as the dimension belonging to organizational culture. Cambra-Fierro and Polo-Redondo (2008) found positive, direct and significant influence of relational aspects of supply chain management on the customer satisfaction. Regarding the given theoretical and empirical grounds it can be concluded that there is an explicit link between SCO and performance outcomes. However, the main idea of this paper is to investigate the link between SCO and purchasing performance outcomes. Hence, the organizational buying

effectiveness (OBE) is applied as a measure of purchasing performance. Up to now there have been several inquiries in measuring the purchasing effectiveness (e.g., Rossler and Hirs, 1996; Janda and Seshadri, 2001) In order to be effective, purchasing should procure the products / services which add value for their customers (forthcoming members of the supply chain) The literature reveals that the most of the supply chain measurement models comprise of financial performance dimensions (Gunasekaran and Kobu, 2007) However, the financial performance is measured on the single firm level and can not be a meaningful measure of the supply chain success. If the financial success of one firm is a result of value stream through the supply chain, than such performance measure is valid. Within this perspective, the dimension of effective purchasing is recognized. The goal of effective purchasing is to provide the value for the forthcoming member of chain. Eventually, a firm that implements the SCO valorizes the role of its purchasing processes in the value creation for customer. Therefore, the following hypothesis is suggested.

H1: Supply chain orientation is directly, positively and significantly related to organizational buying effectiveness.

METHOD

Sample description and research setting

For the purpose of this study a survey was conducted. A self administered questionnaire was developed and questionnaire items were derived and adapted from the existing literature. First, the preliminary interviews with ten members of Croatian Purchasing Association (eight chief purchasing officers and two independent purchasing and supply chain management consultants) were conducted in order to analyze the questionnaire from the perspectives of understandability and practical importance of topic under investigation. Some questionnaire items were modified and further explained which led to its improvement. In the second part of the preliminary assessment, we conducted a pilot test on the sample of 20 chief purchasing officers (CPO) who were also members of Croatian Purchasing Association but did not take part in preliminary interviews. After the pilot test, some items were modified and adapted.

The sample was identified in the Croatian Central firm registry database. Eventually, total sample consisted of 546 medium and large-sized firms. The self administered questionnaire was mailed to the address of chief purchasing officer (CPO) in the firm. Overall, 144 questionnaires were returned from which 21 were not completed. 26 questionnaires did not reach the target address and were returned back. Eventually the effective response rate was 22 % (123 usable questionnaires) which represents a satisfactory rate.

The responding sample firms were from the manufacturing industry. In 2009., the Croatian manufacturing industry accounted for combined \$US 26.42 billion in sales (24 % of total) Sample represented a wide range of manufacturing industries: metal products and metallurgy (13.0 %), engines and machinery (13.0 %), pharmaceuticals (4.6 %), high-tech and electronics (8.3 %), construction products (15.8 %), chemicals, rubber and plastics (9.3 %), textiles and leather (7.4 %), paper and packaging (4.6 %), food (15.8 %) and other manufacturing industries (8.2 %) The key informants were the supply chain management or purchasing executives. The majority of informants occupied positions such as head of purchasing (57.7 %), head of supply chain management (28.4 %), head of sales & purchasing (12.3 %) and other managerial positions (5.6 %).

Next, the test for non-response bias was conducted. The authors have followed the convention of comparing the answers of early and late respondents along the all questionnaire items (Armstrong and Overton 1977) Finally the final sample was split into two groups, depending on the dates they were received. The early group consisted of 60 responses whereas the late group consisted of 63 responses. The t-tests performed on the responses of these two groups showed no statistically significant differences (at 95 % confidence interval) However, two additional tests for non-response bias were conducted. The demographic profile (industry, number of employees and yearly sales turnover) of the non-respondents was not significantly different from the sample firms that responded to a survey. Also, the responding firms exhibited similar demographic properties as the population. These findings lead to a conclusion that no significant non-response bias is present in the survey data.

Measurement operationalization

For the purposes of this study, two scales from the existing literature were adapted. The SCO was measured with the scale adapted from Min and Mentzer (2004). The reported scale consists of 6 dimensions: credibility, benevolence, commitment, norms, organizational compatibility and top management support. The Min and Mentzer's (2004) SCO scale showed respectable dimensionality, reliability and validity estimates. The SCO was modeled as a second order reflective construct.

To measure purchasing performance we used organizational buying effectiveness (OBE) construct. To be effective, organizational buying must proclaim value orientation, insist on higher involvement of other business functions and ensure the sharing of purchasing-related information. Hence, the OBE was measured with three dimensions (constructs): value-oriented purchasing, lateral involvement and information sharing. These constructs have been widely researched in marketing studies. The scales covering OBE dimensions were adapted from the works of Miocevic (2008, 2010) OBE scale also demonstrated acceptable dimensionality, reliability and validity estimates.

Furthermore, the OBE was modeled as a reflective first-order and second-order formative construct (Type II) following the model specifications by Jarvis, Mackenzie and Podaskoff (2003) Empirical examples of modeling and estimating the higher-order constructs in PLS are rarely present in current marketing literature (e.g. Bruhn, Georgi and Hadwich, 2008; Wetzels, Odekerken-Schroder and Van Oppen, 2009; Miocevic, 2010) The first-order dimensions of second-order OBE construct were modeled as reflective, since the nature of indicators thoroughly explains certain OBE dimension. Next, the first-order dimensions were formatively related to the second-order OBE construct. Hence, the combined reflective-formative operationalization of OBE construct is considered to be conceptually and methodologically sound.

Analytical procedure

Because of the small sample size and sufficiently developed theoretical background, partial least squares (PLS) method was used. PLS is a general technique for estimating path models involving

latent constructs that are indirectly observed by multiple indicators. PLS method was developed by Wold (1981) to avoid the need of large sample sizes. PLS enables the simultaneous analysis of the outer (measurement) and inner (path) model. The main reason that PLS fits this research setting is that PLS can estimate the model properties with combined formative-reflective constructs (Chin, Peterson and Brown, 2008) Reinartz, Haenl and Henseler. (2009) suggest that PLS should be used when the sample size is small (but larger than 100) in order to estimate model prediction and to develop a theory.

FINDINGS

First-order measurement model

The measurement model consists of outer model loadings of indicators on the first-order constructs of interest (SCO and OBE dimensions) All indicators have loadings higher than 0.60 to the latent construct they intend to measure (all significant at $p < 0.001$), except the item SCO20 who has a loading of 0.52 which is below the acceptable threshold. Therefore, the SCO20 item was dropped in order to secure a stable and dimensional scale of Top management support. After initial assessment of dimensionality, composite reliabilities (CRs) of all first-order constructs were above 0.85. The CR has advantage over traditional Cronbach's alpha by offering better estimate of the shared variance between indicators (Fornell and Larcker, 1981) Giving the stable factor structure of the measured constructs, the measures exhibit high level of dimensionality and reliability (as the CRs were higher than established standards) (Nunnally and Bernstein 1994) To test for the convergent validity, the average variance extracted (AVE) must exceed a threshold of 0.50 for every construct (Fornell and Larcker, 1981) The Appendix A shows that all constructs have an AVE above critical cut-off value of 0.50. Their respective CRs are greater than 0.70 as suggested by Bagozzi and Yi (1988). The findings confirm convergent validity in this research case, following both conventions, in which all indicators measure the latent construct they intend to measure. To test for discriminant validity, the squared correlation between two constructs must not exceed their respective AVE (Fornell and Larcker, 1981) The highest squared correlation was 0.34 in the case of credibility and norms which does not exceed their respective

AVE. Alternatively, Gaski and Nevin (1985) suggest a test where discriminant validity exists if the correlation among the constructs does not exceed their estimated reliability (reliabilities were above 0.85 for all constructs) In both cases discriminant validity exists. Accordingly, the operationalized first-order constructs do yield dimensionality, reliability, and validity (See Appendix A for further details on measurement properties).

Second-order measurement model

After the assessment of the first-order measurement model, the guidelines for modeling the higher order structural model were followed (Wetzels, Odekerken-Schroder, and Van Oppen 2009): (1) the first-order constructs (dimensions of supply chain orientation) were related to their respective manifest variables (indicators), and (2) the second order construct (supply chain orientation) was related to their respective first order constructs. Table 1 indicates that the critical bootstrap ratios for the loadings of first order factors on second-order factor were all greater than 0,60 and significant at $p < 0,001$.

Assessing indicator colinearity of formative construct

High colinearity complicates the estimation of formative components validity. If the formative indicators correlate perfectly then the information they contain may be redundant. Therefore, in order to achieve formative construct's validity, it is crucial to inspect the variance inflation factors (VIF) of formative indicators. First, the items of three OBE's dimensions were summated as they exhibited more than acceptable composite reliabilities in the assessment of first-order measurement model. Summated scales procedure facilitates

the estimation of model parameters when dealing with small sample data (Mackenzie, Podsakoff and Ahearne, 1998) The summated scales are widely used in social sciences as they are able to generate a good reliability and validity (Spector, 1992) More recently, Ruiz, Gremler, Wahburn and Cepeda Carrion (2008) employed this procedure to inspect external validity of the service value construct in their study. To assess the VIF, the multiple regression was employed, and it seems that all indicators have the VIF value less than 1.8 (See Table 2)

Structural model assessment

All PLS structural models are concerned with two basic questions: (1) what is the amount of variance explained in endogenous variable from the predictor variables, and (2) to what extent do the predictor variables contribute to the explained variance of endogenous variable? In order to reveal these inquiries, in PLS two basic indicators must be considered: β (regression coefficient) and R^2 (explained variance in the endogenous variable) R^2 is the measure of predictive power just as in the regression analysis and to be satisfactory, its estimated value must be 0.1 or greater. These indicator estimates are somehow substitute for the fit indices offered by covariance based methods (LISREL and AMOS)

To estimate the structural relationships, we employed the bootstrapping method (500 re-samples) to generate standard errors and t-statistics. As for the structural model assessment, the critical bootstrap ratio (t-value) in the SCO - OBE link ($\beta = 0.612$) was 6.26 ($p < 0.001$), followed by the R^2 of 0.375, which leads to the acceptance of H1, stating that SCO directly influences the OBE. The results are depicted in the Figure 1.

Table 1: Second-order measurement properties

Second-order factors	Loadings	P
Supply chain orientation		
<i>Credibility</i>	0,71	<0,001
<i>Benevolence</i>	0,75	<0,001
<i>Commitment</i>	0,77	<0,001
<i>Norms</i>	0,76	<0,001
<i>Organizational compatibility</i>	0,74	<0,001
<i>Top management support</i>	0,74	<0,001

Table 2: Multicollinearity assessment

Dimension	VIF	Weight
Lateral involvement	1.80	0.414
Information sharing	1.49	0.393
Value-oriented purchasing	1.64	0.401

DISCUSSION

The findings of this study confirm that the relationship between SCO and OBE is direct, positive and significant. The findings of this study imply the growing importance of relational antecedents in supply chain management and as well their impact on the performance outcomes such as the OBE. OBE should not be considered as an ultimate performance outcome. Rather, OBE is a catalyst that secures the value flow throughout the supply chain. Early literature has considered purchasing as a secondary value chain activity with no strategic relevance for the contemporary firm (Porter, 1998; Ramsay, 2001). Conversely, this study challenges this agenda and implies that role of purchasing is to provide a value for the forthcoming member of

the supply chain. SCO validates the importance of viewing the supply chain members as partners in the value creation process for ultimate customer. In the case of applying the SCO as a relational capability, purchasing opts to become a primary activity which directly impacts on the value creation process for customers. Hence, the SCO should be considered as crucial organizational capability which builds the competitive advantage of all firms enrolled in supply chain. SCO capability can be developed when chain members share common values and beliefs that are focused on viewing the supply chain as an integrated business system and not just on their specific business processes.

Figure 1: Structural model properties



CONCLUSIONS

SCO has shown to be the vital organizational capability which endorses a relational view of supply chain relationships. SCO is considered to be a capability created by relational capital which is developed within the perspective of supply chain relationships. Findings of this study suggest that SCO implementation has a positive effect on the OBE. However, Mentzer, Min and Zacharia (2000) warned that firms must be careful when implementing any means of relational aspects in managing the supply chain. Thus, firms must differ between strategic (long-term) and operative (transactional) partnerships in the supply chain. Not all relationships should be treated equally, because all members of the supply chain organization do not add value in the same extent. Therefore, future studies could contribute by investigating the difference between strategic and

transactional suppliers in the contribution to value-adding processes for business customer.

Further research should integrate both perspectives of SCO – relational (Min and Mentzer, 2004) and cultural (Hult et al., 2008) Recent work by Esper, Defee, and Mentzer (2010) suggested such integration by providing the conceptual ground for future investigation of this crucial supply chain capability.

The SCO's positive influence on the OBE suggests that purchasing has a rather different goal when considered within a supply chain context. However, this study has only partially succeeded to address the issues regarding the role of purchasing activities in supply chain context. Further studies should explore the OBE's link with other performance indicators. In this manner, the nomological network could be enriched by incorporating

various perceptual performance measures (e.g. customer satisfaction and loyalty). Extension of OBE's nomological network would offer a more clear evidence of purchasing's role and influence in the value creation process for customer.

Self reports based on single sample data may not be an appropriate means of empirical inquiry in the supply chain context. Future studies could investigate how other roles in organizational buying (e.g., users and influencers) respond when considering the SCO and its influence on purchasing behaviour. Earlier studies have found that different roles in organizational buying have different views on purchasing issues (Chakraborty, Srivastava and Marshall, 2007).

Notably, future studies could reveal other possible avenues of the SCO and OBE in greater detail by employing a qualitative research design. An in-depth approach would contribute would enrich theoretical content of these constructs.

Managerial implications of this research are evident. SCO, based on the relational dimensions confirms the importance of socio-psychological antecedents in managing the upstream and downstream flows in supply chain. The positive link with OBE confirms that purchasing managers should nurture SCO which will develop supply chain visibility. Visibility ensures that focal firm valorizes the role of other supply chain members in the value creation for ultimate customer.

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NETWORK THEORY AT MOBILE PROVIDERS

ÁGNES LUBLÓY
CORVINUS UNIVERSITY OF BUDAPEST, HUNGARY

Abstract

Network theory represents a powerful tool to study the behaviour of mobile phone users concealed in the call records collected by mobile operators. Network theory might function as an important value driver, a crucial organizational capability that provides the companies competitive advantage. The author surveys the existing literature and describes various business applications to demonstrate how network theory could deliver additional value to today's telecommunication companies. At first, the role of advanced community detection methods in promoting customer segmentation, customer acquisition, product pricing and group-based marketing initiatives is shown. Then the author argues that the network value of customers should not be neglected in measuring the lifetime value of customers. Network neighbours might exert significant influence on their contacts; a network effect upon which the mobile providers should play proactively. Business applications exploiting the influential role of network neighbours include customer behaviour prediction (handset uptake, choice of mobile provider, etc.), customer churn and viral marketing. Finally, the role of network theory in missing data estimation and product development, such as location aware services, is emphasized.

Keywords: network theory; business applications; communities; customer lifetime value; customer behaviour prediction; churn; viral marketing; missing data estimation; location aware services

1. Introduction

The mobile phone has become an integral part of our everyday life. The call records collected by mobile operators represent a powerful tool to study the behaviour of mobile phone users. Exploring the behaviour of mobile customers might explain

various real-world phenomena and create value for service providers. Social network analysis, which has emerged as a key technique in the intersection of modern sociology and information sciences, is a promising tool for enhancing our understanding of phenomena such as provider choice, customer acquisition, customer retention, customer churn, spreading of news or diffusion of product developments. With regard to business, gaining knowledge about these phenomena may permit the mobile provider to gain and maintain its competitive edge more efficiently.

The primary goal of the author is to demonstrate how network theory could deliver additional value to today's telecommunication companies. Network analysis might function as an important value driver, a crucial organizational capability that provides the companies competitive advantage. The author surveys the existing literature and describes various business applications to demonstrate the role of network theory in value creation. The surveyed articles are mostly written by physicists or computer scientists and might be out of sight for telecommunication managers. With the aim of drawing the attention of telecommunication experts on the most recent research advances of the field, the author demonstrates the value creating role of network theory in seven business areas.

The organization of the article is as follows. Section 2 demonstrates the role of advanced community detection methods in customer segmentation, customer acquisition, product pricing and group-based marketing initiatives. In Section 3 the author argues that marketers should add the network value of customers to the traditional customer lifetime value in order to capture the influence of customers on their network neighbours. In Sections 4 to 6 business opportunities exploiting the influence exerted by the network neighbours on their contacts are considered. Section 4 illustrates how useful information about the network neighbours

might be in predicting customer behaviour, such as, handset uptake, choice of mobile provider or usage of specific mobile phone functions. Section 5 highlights the importance of network neighbours in customer churn by reviewing the most recent strand of churn management literature. Section 6 focuses on viral marketing, a technique that leverages the customers themselves to carry out promotional effort. Section 7 stresses the role of network theory in missing data estimation; while Section 8 highlights how the availability of location and mobility data has enabled the development of location aware services. Finally, Section 9 provides the conclusions.

2. Community structures

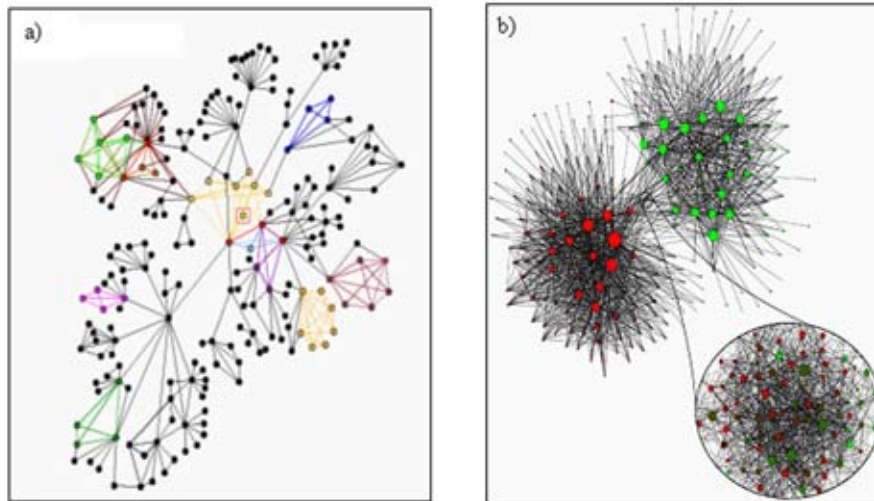
Call records can be easily translated into a social network that captures the characteristics of the underlying communication network. Prominent papers exploring the network topological properties of mobile communication networks and their social consequences include, for example, Lambiotte et al (2008) and Onnela et al (2007a, 2007b). The most well-known characteristics of large-scale communication networks include the skewed degree distribution with a fat tail, the small-world property, a typically much larger clustering coefficient than in the comparable random networks, degree-wise assortativity, link weights depending on the relative proportion of common neighbours (link overlap) and tie-strength distribution with wide variability and heavy tail.

Another important characteristic of social networks that have been found to occur commonly includes the existence of communities. A social network shows community structure if it divides naturally into groups of individuals with dense connections within groups and sparser connections between groups. Communities within a mobile network might include, for example, individuals with

similar hobbies or socioeconomic status. Figure 1 provides insight into the community structure of two mobile phone networks. The inherent tendency to cluster is shown in Fig. 1a on a local level, while Fig. 1b reflects a global perspective encompassing the majority of the nodes within one of the communities.

Advanced community detection methods might support various marketing initiatives of mobile providers. In the following paragraphs five application possibilities are considered. Customer segmentation, the method of grouping customers based upon similarities, is an obvious candidate for applying sophisticated community detection methods. The practice of dividing the customer base into groups of individuals that are similar in specific ways relevant to marketing, such as age, interests, usage behaviour or spending habits, is the precondition for several marketing decisions. Customer segmentation can be a powerful means to design an optimal distribution strategy, to create product differentiation strategies, to develop tailored customer servicing or to determine adequate product pricing. Customer segmentation, supported by sophisticated community detection methods, is also the prerequisite for direct marketing of groups. In sum, combining the traditional customer segmentation techniques with the innovative community detection methods can help mobile providers to extract maximum value from customers through developing efficient marketing initiatives.

Community detection might also promote the acquisition strategy of mobile providers. In acquisitions a relatively easy way to increase the customer base is to convince competitors' subscribers to switch through member-get-member type promotions. In these promotions the target campaign list should be community-based.

Figure 1: Community structures in mobile phone networks

Source: Palla, Barabási and Vicsek (2007), Figure 1b.

Third, knowledge about communities might be useful for establishing an optimal pricing policy. Pricing of a product is an important step in merchandising, in which both the quality of the product and the demand plays a vital role. In the telecommunication industry, due to significant network externalities, communities should also be considered as an important pricing factor. (The price benefit obtained by the subscribers joining the same mobile operator is analyzed in Gerpott (2008) in detail, along with the effects of on- and off-net price differentials on subscription decision and calling behaviour.) Nowadays customers are becoming more and more community-conscious and start to demand value for money through community-based pricing. As the delicate pricing of a product is an important factor in fighting off competitors, mobile operators should offer communities, identified by means of community detection methods, reduced prices that satisfy the needs of their community-conscious members. The business practice of offering reduced prices for well-defined communities, such as families and companies, has been followed by the majority of the operators. For example, T-Mobile, the largest mobile provider in Hungary, targets its Family-friendly package at family members, its You and me or Domino Friends package at friends, while its Etalon, Etalon Team, Success Pluss, etc. packages at companies.

Fourth, when experts estimate a customer's lifetime value, several aspects of the community in which the customer is embedded should be taken into account. In the telecommunication industry, being an industry with significant network effects, the value of customers should not be determined on a stand alone basis. The network aspects of estimating a customer's lifetime value are discussed in Section 3.

Finally, community detection methods, combined with the a priori knowledge about customers, might also help experts to identify receptive communities whose members will adopt a new product or service with the highest probability. Making exclusively the receptive and influential customers familiar with the new product is very cost effective as it leverages the customers themselves to carry out promotional effort. This phenomenon, referred as viral marketing in the literature, is discussed in detail in Section 6.

Finding communities within a large-scale social network is a challenging task. The number of communities is typically unknown and the communities are often of unequal size and density. Besides numerous algorithms, various aspects of community-detection methods are discussed in the reviews of Newman (2004), Danon et al (2007), Schaeffer (2007), and Porter, Onnela, and Mucha (2009). The recent study of Fortunato

(2010) provides a comprehensive overview of community detection methods, with a special focus on techniques designed by statistical physicists. The majority of the traditional and modern methods aim at detecting standard partitions, that is, partitions in which each node is assigned to a single community. However, in real graphs nodes are often shared between communities. The fact that several actual networks are made of highly overlapping cohesive groups of nodes inspired the research of detecting overlapping communities. In the field the clique percolation method developed by Palla et al (2005) became by far the most popular.

In the literature, to the author's knowledge, three studies detect communities in mobile phone graphs. Blondel et al (2008) propose a new, clustering-based community detection method that reveals the hierarchical community structure of networks. By applying a fast hierarchical modularity optimization technique to the network of 2.5 million Belgian mobile phone customers, the authors identify communities that reflect the linguistic split of the Belgian population (see Figure 1b). From a business point of view, detecting homogeneous communities might help the mobile providers to target tailored marketing campaigns at them.

By analyzing calls between mobile phone users Palla, Barabási, and Vicsek (2007) investigate the time dependence of overlapping communities on a large scale. The authors discover fundamental differences between the dynamics of small and large groups. They find that large groups persist for longer if they are capable of dynamically altering their membership. The behaviour of small groups displays the opposite tendency; the condition for stability is that their composition remains unchanged. The authors also show that knowledge of the time commitment of members to a given community can be used for estimating the community's lifetime. Mobile providers might translate the above findings into money by identifying stable communities, let it be small or large, and targeting group-based, long-term loyalty programs at their members. At the same time, quickly evolving communities should be targeted for group-based, short-term contracts.

Using the same dataset as Palla et al (2007), Onnela et al (2007b) investigate the role of weak and strong ties within and among communities. The authors find that strong ties are predominantly within communities, and their removal will only

locally disintegrate a community but not affect the network's overall integrity. In contrast, the removal of weak links will delete the bridges that connect different communities, leading to a phase transition driven network collapse. Thus, strong ties play an important role in maintaining local communities, while weak ties appear to be crucial for maintaining the network's structural integrity. The above findings are also supported by Dasugupta et al (2008). As for business application, strong ties are important for diffusing news and innovations within a community, while weak links play a crucial role in spreading information across communities. The benefit that mobile providers might realize from the distinction between weak and strong ties is discussed in Section 6 in relation to viral marketing.

3. Customer lifetime value

In the marketing literature customer lifetime value (CLV) is defined as the present value of the future cash flows attributed to the customer relationship (see e.g., Kumar, 2007). The metric represents how much a customer is worth in monetary terms over a period of time. The marketing concept places greater emphasis on customer service and long-term customer satisfaction, rather than on maximizing short-term sales. Singh and Jain (2009) provide an excellent overview of the literature related to CLV measurement, while Hwang, Jung, and Suh (2004) and Pynnonen and Hallikas (2008) specify CLV models for mobile providers.

Domingos and Richardson (2001) distinguish between the intrinsic and the network value of customers. The intrinsic value of a customer, in line with the traditional definition of CLV, is based on the sales revenue an organization expects to realize from the customer. In contrast, the network value of a customer is related to the customer's influence on others' probabilities of purchasing the product. In a similar vein, Kumar, Petersen, and Leone (2007) define the customer's referral value as an estimate stemming from referrals. In the presence of strong network effects the ignorance of the network (referral) value might result in incorrect marketing decisions. A customer whose intrinsic value is less than the cost of marketing may in fact be worth marketing to when the customer's network value is considered, that is, his influence on his friends, their influences on their friends, and so on. Similarly, if strongly linked customers realign their choice of provider to an

opinion-leading customer, then some part of the followers' customer value should be added to the opinion leader's lifetime value. Note that detecting the communities in which the customers are embedded (see Section 2 for details) is essential for calculating the network value.

Nowadays marketers put an ever stronger emphasis on estimating the CLV accurately. As a result, the network value of customers has become a well-established measure both in the academic world and in corporations. Hogan, Lemon, and Libai (2004), for example, provide a simple approach to the measurement of post-purchase word-of-mouth (WOM) sales effects. The authors quantify the WOM multiplier that shows the multiplicative difference between the value of an advertisement taking the ripple effects into account and the value of the advertisement without WOM. Gupta and Mela (2008) assess the customer value when two parallel populations (e.g., buyers and sellers) interact and have strong direct (within population) and indirect (across population) network effects. Domingos and Richardson (2001) propose a model in which each customer's probability of buying is a function of both the intrinsic desirability of the product for the customer and the influence of other customers. They find that the network value of customers follows an exponentially decaying function: a few customers have an extremely high impact on the network neighbours. The authors also identify the characteristics of customers worth marketing to and estimate the value of justified customer acquisition cost. Further prominent papers incorporating the network value of customers in the CLV measurement include, for example, Hogan, Lemon, and Libai (2003); Ho, Li, and Shen (2010). All articles cited in this paragraph, however, suffer from two shortcomings: the analyses are neither telecommunication specific, nor rely on a real social network. In the following paragraphs the first shortcoming is addressed by reviewing two papers. To the author's knowledge, papers other than these two have not been published until now.

Telecommunication specific valuation insights are provided in the work of Lee, Lee, and Feick (2006). The authors incorporate the impact of WOM on CLV through the direct savings of acquisition cost of customers accrued by the market growth, and through the variation of acquisition cost to replace churning customers. Although the surveyed customers do not form a network and the actual

data should be complemented with several other estimates, Lee, Lee, and Feick (2006) could highlight the importance of WOM in markets with high growth rate and intense competition. Their simulation results show that in the segment of low revenue and high WOM, CLV is increased by 102 per cent per customer, and the contribution of WOM to CLV is raised from 11 to 18 per cent.

Telecommunication specific questions are also addressed by Liu et al (2009). The authors propose a customer network value model, in which the value stems from the influence value and the existence value (customer's contribution to the network structure). As for criticism, the basic model setup and the small, loosely connected network result in primitive calculations.

Despite the huge advances in the availability of customer transaction and billing data, to the author's knowledge, no scientific work uses large-scale network data extracted from call details to measure the network value of customers in the telecommunication industry. This shortcoming is clearly an area for future research that requires the collaboration of physicists and marketers. Especially, as the metric of CLV incorporating both the intrinsic and the network value of customers might support various marketing initiatives and create additional value for mobile operators. First, CLV provides an excellent orientation how much the marketing department should spend as a maximum to acquire a new customer. In line with the network value of customers, the extensive friendship circle of the target customer should also be taken into account, as the friends of the target customer might also switch operators. Note that acquiring a customer, who has many friends within the network of the operator, but so far no subscription with the company, should be a relatively easy and lucrative marketing action. Secondly, CLV might be a useful tool for pricing various products and services. Keeping the network relations of customers in mind, an optimal pricing policy allures many customers from the competitors while increasing profit. Thirdly, CLV plays an important role in churn management. The metric incorporating the network value of customers shows the potential losses associated with the churn, and provides the most accurate estimate of the maximal budget to spend on retainment efforts. The provider's retainment budget might be much higher than the one predicted on the basis of the intrinsic value of customers, especially if the initial

churn results in an avalanche of service switching. (Due to the importance of churn management in the telecommunication industry, this topic will be discussed in Section 5 in detail.) CLV might support several other business applications. Kumar (2007) develops altogether eight customer-centric strategies in which the traditional CLV measure is remunerative. Note that the customer-centric strategies of Kumar (2007) are easily adaptable to the CLV metric that also incorporates the network value of customers.

4. Customer behaviour prediction

This section illustrates how useful information about the network neighbours of customers might be in predicting customer behaviour more accurately. The author reviews briefly those recent articles in which social network data proved to be helpful in predicting service or device uptake among mobile communication customers.

Kiss and Bichler (2005) argue that mobile providers should incorporate network-related measures in the models supporting their Customer Relationship Management (CRM) applications. The authors show that analysts can achieve higher accuracy in predicting customer behaviour by exploiting information about customers' interaction in the call network. They build upon the hypothesis that subscribers with specific usage behaviour might have similarly behaving users in their neighbourhood. More precisely, the authors assume that the SMS (Short Message Service) usage of customers also depends on the texting habit of their network neighbours. The researchers find that the accuracy of the behaviour prediction model improves significantly when the attributes of both the customers and their neighbours are incorporated in the models.

The findings of Maicas, Polo, and Sese (2009) also provide important insights into customer behaviour. Among others, the authors investigate the role of personal network effects in explaining customer choice in the Spanish mobile telecommunications industry. Their results reveal that personal network effects play a key role in determining mobile users' choice: the probability that a customer selects a mobile phone company increases with the number of members of her social network already subscribed to that firm. Concerning the drivers of customer choice, the authors find that relationship characteristics (length, depth and breadth) and

demographics differently affect personal network effects perceptions.

The research plan of Reid and Hurley (2010) is also promising in terms of customer behaviour prediction. Having information on the handset currently used by each user, the authors plan to measure the impact of social effects on handset uptake. They plan to investigate whether the social dimension plays a significant role in the spread of changes in handset adoption.

Recent research has clearly shown the role of network effects in customer behaviour prediction. The finding that customers exert significant influence on their network neighbours is evidently transferable to several other analytical CRM applications, such as phone package choice, product preferences, usage of innovative mobile phone functions, service usage and churn management. Due to the major threat imposed on profit margins, the latter application is discussed in the next section in detail.

5. Churn management

Mobile providers face the phenomenon of churn, that is, the loss of subscribers who switch from one provider to another, on a daily basis. In the endeavour to expand the customer base, or at least maintain the number of customers at a constant level, the providers must stay on their toes in a fierce competition for customers. As attracting new customers is more expensive than retaining old ones, churn management is a fundamental concern. In order to keep the number of switching customers at a minimum, mobile companies must identify the customers at risk and target tailored marketing campaigns at them.

In the past researchers tended to employ survey data to identify the determinants of subscriber churn and customer loyalty in the mobile telecommunications market (see e.g., Gerpott, Rams, & Schindler, 2001; Kim and Yoon, 2004). Over time, thanks to the increase in computational capacities, it has become possible to complement survey data with actual customer transaction and billing data for research purposes. In general, the analysts developed solid and accurate churn models by applying sophisticated classification techniques, such as logit models, decision trees and neural networks (see e.g., Mozer et al, 2000; Wei and Chiu, 2001; Ahn, Han, & Lee, 2006).

The data mining methods of traditional churn models disregard the network effect; the value of each customer is determined on an individual basis. However, if one key customer switches from one service provider to another, several customers having strong links to the key customer may do the same. Should this process start an avalanche of service switching, the provider's loss will be far more substantial than originally predicted. In the most recent strand of churn management literature the researchers reckon with the potential spill-over effects resulting from social linkages between customers and identify the influence from network neighbours as an important determinant of customer churn. The latest findings of the field are discussed in the follow paragraphs.

Dierkes, Bichler, and Krishnan (2009a) analyze the influence of churners on their network neighbours. The authors apply Markov logic networks for churn prediction and show that building upon the information of the network neighbours' churn results in a significantly higher predictive accuracy and sensitivity. In a recent symposium the researchers argue (Dierkes, Bichler, & Krishnan, 2009b), that the simple heuristic of selecting churners first, and then analyzing their communication traits, can reveal useful information for a marketer to design win-back campaigns.

Dasgupta et al (2008) predicts potential churners by examining the communication patterns of millions of mobile phone users. The authors use a spreading activation-based technique and view the behaviour of churn as a diffusion process. The analysis explores the propensity of a subscriber to churn out of a service provider's network as a function of the number of friends that have already churned. Dasgupta et al (2008) provide substantial evidence that social relationships play an influential role in affecting churn in the operator's network. The authors find that the churn probabilities increase if an individual has friends who have churned in previous months, hinting towards a cascading effect of these influences. In addition, the researchers conclude that the probability of churn is not only affected by the number of churning friends that one has, but also the local topology connecting these friends.

Finally, Benedek and Lublóy (2010) argue that mobile companies should update their churn models by the addition of some network related metrics. Besides allowing a longer-term projection of churners, the inclusion of network-

related measures also improves, even in the short run, the accuracy of the churn model. The authors investigate the essential question of whether a substantial difference exists between retained and churned customers in terms of network characteristics. In the study meaningful segmentation is achieved with reference to seven network topological properties capturing the number of relations and the embeddedness of customers. The study provides clear evidence that individual network characteristics have a considerable impact on churn probabilities. The analyses also reveal that customers targeted by direct marketing campaigns are less threatened by churn than are their non-targeted peers, which highlights the importance and effectiveness of the provider's marketing actions.

The problem of churn modelling does not end at this stage, however. Once the importance of network topological properties of customers in churn modelling have been realized, building them into existing churn models is of major importance. Evaluating the additional explanatory power of the network measures should follow next. Several classifications methods, such as logistic regression, decision trees or neural networks, are available as tools of ranking the variables according to their explanatory power.

6. Viral marketing: spreading of news and innovations

Diffusion of innovations, the process by which an innovation is communicated through certain channels over time among the members of a social system, has been studied by sociologists over decades. Rogers (2003) provides an excellent overview of this diffusion research. Recently a number of important breakthroughs have been made by network scientists while studying diffusion of epidemics and rumours over networks (see e.g., Newman, Barabási, & Watts, 2006).

Keeping in mind that the primary purpose of mobile phones is information transfer between two individuals, news and rumours might diffuse within communication networks, occasionally reaching a large number of individuals. Marketing messages might also disperse through communication networks. The most important difference between the propagation of viruses and the spreading of marketing messages is that virus infection can be cured, while once a message is received,

the customer remains infected (Kiss and Bichler, 2008). In addition, the marketing signals decay in the function of the age of the message. Once the message starts to become outdated, the text is forwarded to a lesser extent.

As word-of-mouth (WOM) communication has an enormous impact on customer opinions and buying decisions, marketing departments focus more and more on influential customers. Marketers use viral marketing methods to profit from the WOM communication among their customers. The WOM advertising is more cost effective than traditional marketing methods, such as direct marketing or mass marketing, since it leverages the customers themselves to carry out promotional effort. Viral marketing encompasses all the techniques that build upon the social relations of customers to increase the brand or product awareness by viral diffusion process, analogous to the spread of epidemics or computer viruses (Kirby, 2006). Viral marketing rests on the idea of a campaign reaching a „susceptible” customer, who becomes „infected” and then starts infecting other susceptible users. Viral marketing is an efficient tool to reach a large number of customers rapidly, especially if the campaign is targeted at influencers, that is, opinion-leading customers. Despite the huge advances in the viral marketing literature (see e.g., Goldenberg, Libai, & Muller, 2001; Leskovec, Adamic, & Huberman, 2007; Palka, Pousttchi, & Wiedermann (2009); Trusov, Bodapati, & Bucklin, 2010) in the following paragraphs, for the sake of brevity, only studies dealing with diffusion processes on mobile call graphs are reviewed.

Currently operators predict the likelihood of using a particular service, such as SMS or MMS, on the basis of scoring models. Kiss and Bichler (2008) argue that marketers might stimulate the usage and boost profit more efficiently, if the outcome of the scoring model is combined with centrality measures. Centrality measures might provide guidance for marketers to select those customers, who not only have a high likelihood of forwarding a message, but whose position in the network allows them to reach a large number of other customers. Kiss and Bichler (2008) compare different centrality measures with regard to the diffusion of marketing messages. The authors, similarly to Kempe, Kleinberg, and Tardos (2003), explore the essential question of which centrality measures should be used for selecting an initial set of customers for a marketing campaign in

order to achieve a maximum dissemination of messages. When the initial set of customers was chosen according to SenderRank and out-degree measures, the number of reached customers was substantially higher than selecting the initial set of customers according to other centrality measures. Thus, the designer of a marketing campaign should use these metrics to achieve the widest dissemination of marketing messages.

Onnela et al (2007a) study the diffusion of news and rumours on a weighted mobile call graph. As individuals within communities tend to be linked via strong ties, whereas communities tend to be connected to other communities via weak ties, the diffusion of information follows a special pattern. The authors observe rapid diffusion within a single community, followed by plateaus, corresponding to time intervals during which no new nodes are infected before the news escapes the community. The authors argue, that both weak and strong ties are ineffective, when it comes to information transfer, the former because the small amount of on-air time offers little chance of information transfer, and the latter because they are mostly confined within communities, with little access to new information. The authors conclude that contrary to the classical weak tie hypothesis of Granovetter (1973), in the vast majority of cases an individual learns about the news through ties of intermediate strength. As for business, the findings of Onnela et al (2007a) suggest, that mobile providers should target advertisements at customers being connected to others through ties of intermediate strength. These customers are the most efficient in spreading marketing messages within a social network, and therefore play a crucial role in promoting the adaption of innovative product developments.

Szabó and Barabási (2006) investigate the spread and usage of four mobile phone-based services. The authors find that service usage is characterized by detectable dyadic effects, that is, if a customer uses a specific service in a regular fashion, his or her phone-based contacts will also use it regularly. However, the magnitude of the dyadic effect is service-dependent. Chat and MyFriends, defined as cooperative services, display a strong community-based segregation and high dyadic effect. In contrast, Email and WAP, labelled as individual services, are characterized by weaker dyadic effect and absence of compact user communities. With regard to business applications,

Szabó and Barabási (2006) explore the impact of advertising and incentives on service usage. The researchers find that in a saturated market traditional marketing techniques are ineffective in permanently boosting the customer base: once the incentive is removed, the number of users returns to the pre-incentive value. In contrast, hub-based incentives might permanently boost the usage of cooperative services. Thus, telecommunication experts should identify the right class to which a service belongs to and design hub-based incentives only for cooperative services.

Having in mind the role of social network in service usage, Szabó and Barabási (2006) also develop an analytical model to predict the adoption rates for various services. Their model accurately describes the usage dynamics observed in the past. As for money making, mobile providers might use this modelling framework to predict future adoption rates more accurately, which would enable them to reallocate resources to the most promising product developments.

7. Estimation of missing customer data

Accurate customer demographic data is essential for mobile providers. Carrying out efficient marketing campaigns, backtesting the outcome of mass marketing initiatives or evaluating the competitors' action require up-to-date customer demographic data. As incomplete customer demographic database poses limits to customer relationship management, estimation of missing customer data is of major importance. Figure 2, inspired by conversations with Gábor Benedek, highlights the role of network theory in missing data estimation.

Missing value imputation procedures have been extensively discussed in the social science literature, for a review see, for example, Schafer

and Graham (2002). The most popular methods of maximum likelihood and Bayesian multiple imputation, however, do not count with the information obtainable from social linkages. To the author's knowledge Stoica et al (2010) is the only work that provides network theoretical insights into missing demographic data estimation in the mobile communications industry. In the following paragraph the most important findings of that research is highlighted.

The results of Stoica et al (2010) indicate significant differences in mobile usages both by gender and by age. The researchers study the relation between the customers' age, gender, calling patterns and profiles based on topological properties of ego-centred networks. The authors observe different ego-centred networks in the function of the age. Middle aged people are generally involved in sparser structures, while younger and older groups are more densely connected. However, the youngest belong to some cliques, while the oldest keep a very densely connected small network. At the end, the authors could observe four main homogenous age groups similar to life style categories. Stoica et al (2010) also found that phone calls towards a woman are longer than calls to a man, whatever the gender of the caller is. Finally, they showed that with age the network of male mobile subscribers start to become predominantly composed of female. In sum, the authors found very different behaviour depending on the age of the users and their gender. From a practical point of view, the above findings support the estimation of missing demographic data. In addition, the results highlight the potential for different diffusion and WOM patterns for different genders and age groups with which viral marketers should reckon.

Figure 2: Customer data estimation

Source: Blondel et al (2008), Figure 2.

8. Location aware services

The capture and availability of location and mobility data has enabled the development of many location-based or location aware services. Location-aware advertising (also known as mobile advertising or proximity-based advertising) is emerging as one of the most promising business opportunities. Gidófalvi, Larsen and Pedersen (2008) make an attempt to empirically estimate the capacity of the mobile advertising channel. The authors conclude that location based advertising has a huge marketing potential: within a single day 100 mobile ads per user is a realistic scenario. At the same time their results indicate the need to incorporate user-control of the received mobile ads (number of messages, time and place of delivery). Mobile operators might fulfil a special role in mobile advertising. Having mobility and demographic data at their disposal, they might predict which customer will enter a given shopping centre and sell this information. But how much might a mobile operator ask for this kind of information? Using insights from cell phone data, Baccelli and Bolot quantify the economic value generated by mobile users with location based services (Bolot, 2010). The authors determine the value of location information for different granularities, for example for the GPS location of a mobile user, for the access point, and for the cell tower, with which the user is associated. The model of the authors can be used as decision making tools for entities interested in or involved in the location data economics chain, such as mobile operators or providers of location aware services.

Besides proximity-based advertising location-aware social network services might be also a lucrative business idea. Such services offer the possibility of keeping track the location of our friends and acquaintances. Mobile phones might incorporate this kind of service easily. The recent study of Kofod-Petersen, Gransaether and Krogstie (2010), among others, address the question whether students attending a three-week student festival are willing to disclose location information to their friends in a large setting, such as citywide. The main findings show that 55% of the students are ready to use such systems on larger scale, however, the possibility of turning off the system is found to be important. The authors also point out that privacy and trust-oriented issues are crucial for this type of service, such as the quick establishment of a substantial user-base.

Additional recent location data applications include, for example, the prediction of leisure preferences for people living in a particular location (Calabrese et al, 2010), and the identification of urban usages and the relative audiences for various festival events (Cariou, Ziemlicki, & Smoreda, 2010). With regard to business, mobile providers might pocket some extra cash by selling location data at their disposal in compliance with privacy requirements.

9. Conclusions

Bolot (2010) mentions that recently a number of companies and research groups worldwide have started analyzing a growing variety of data including social network data (who calls whom, how often), location and mobility data (where users are),

and spectrum usage data (who uses how much spectrum in which cell). Several articles suggest that mobile customer's decisions are influenced by their social network. In this article the author showed that the knowledge and exploitation of the social influence might permit the mobile providers to gain and maintain their competitive edge more efficiently. The author also argued that transforming the knowledge about personal network effects into valuable business applications required sophisticated methods, such as the ones offered by network theory. In this article seven business areas were covered to demonstrate the value creating role of network theory. The key message from each business area is as follows:

- Communities overlap and evolve in time. Mobile providers should target group-based, long-term loyalty programs at stable communities, while group-based, short-term contracts should be offered to quickly evolving communities. Advanced community detection methods might promote customer segmentation, customer acquisition, product pricing and group-based marketing initiatives.
- The network value of customers should not be neglected in measuring the lifetime value of customers. Network neighbours might exert significant influence on their contacts; a network effect upon which the mobile providers should play proactively.
- Mobile providers should exploit the influential role of network neighbours in predicting customer behaviour, such as handset uptake or choice of mobile provider.
- Churn models should not disregard the obvious network effects. Modelling churn as a diffusion process is a promising research area.
- Viral marketers should target advertisements at customers being connected to others through ties of intermediate strength.
- Recent research revealed significant differences in mobile usage both by gender and by age, highlighting the role of network theory in missing data estimation.
- The availability of location and mobility data has enabled a number of new services and economic activities, among other proximity-based advertising.

Network theoretical methods might function as an important value driver within a wide range of business applications. In this article the author considered seven business areas, however, the number of possibilities might be much more. At telecommunications companies network theory might inspire new business applications on a daily basis, requiring the collaboration of marketers, economists, physicists and computer scientists. With the aim of boosting profit, business solutions are tailored to the needs of the company and are strictly confidential. Solutions hidden from the public might include promising product developments or the identification of key sales managers, risk bearing customers or employees.

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PROMOTION OF HEALTH TOURISM IN THE KVARNER REGION

BRANKA BERC RADIŠIĆ

FACULTY OF TOURISM AND HOSPITALITY MANAGEMENT, OPATIJA

LORENA BAŠAN

FACULTY OF TOURISM AND HOSPITALITY MANAGEMENT, OPATIJA

JASNA LASINGER

FACULTY OF TOURISM AND HOSPITALITY MANAGEMENT, OPATIJA

ABSTRACT

That well-conceived promotion can yield good results in a very short time is evident in the case of Croatia, which was listed among the ten most desirable destinations in the world in 2010. The successful promotion of any destination is reflected in the number of its tourist arrivals and the volume of tourist spending, as well as in the demand for diverse segments. This paper deals with a particular segment of tourism, specifically health tourism. By keeping abreast of trends on the European and world tourist market and in response to the growing demand for health-related services and facilities in tourism, Croatia has adopted new strategies and has designed health tourism and wellness tourism offerings. This paper looks at the current situation of and results achieved in health tourism in Croatia, as well as the trends in and performance of the tourism offering. The performance of health tourism in the Kvarner region is examined. The main body of the paper deals with the promotion of health tourism in the Kvarner region and the way in which health tourism is incorporated in the destination's tourism product. The last part of the paper puts forward proposals and suggests measures aimed at further improving the promotion of health tourism in the Kvarner destination.

Key words: Kvarner, tourism product, destination, promotion, wellness,

SAŽETAK

Da se uz kvalitetnu promociju rezultati mogu postići u vrlo kratkom vremenu, vidi se na primjeru Hrvatske, koja je prošle godine uvrštena među

10 najpoželjnijih destinacija u svijetu. Kvalitetna i uspješna promocija određene destinacije ogleda se u rezultatima posjećenosti turista i njihove potrošnje u destinaciji kao i potražnje za raznolikim segmentima. U ovom radu govori se određenom segmentu turizma točnije zdravstvenom turizmu. Praćenjem trendova na europskom i svjetskom turističkom tržištu te sve većom potražnjom za zdravstvenim sadržajima u turizmu Hrvatska donosi nove strategije te odgovara na to pitanje kreiranjem ponude zdravstvenog i wellness turizma. U radu daje se prikaz i rezultati sadašnjeg stanja zdravstvenog turizma u Hrvatskoj, kretanje i uspješnost turističke ponude. Kao primjer destinacije navodi se Kvarner gdje se promatraju rezultati uspješnosti zdravstvenog turizma. Kao glavni dio rada navodi se promocija zdravstvenog turizma na području Kvarnera te pregled na koji način se ona uključuje u sveukupni turistički proizvod destinacije i plasira na tržište. Posljednji dio rada sadrži pregled prijedloga i mjera za daljnje unaprjeđenje promocije zdravstvenog turizma destinacije Kvarner.

Ključne riječi: Kvarner, turistički proizvod, destinacija, promocija, wellness,

INTRODUCTION

Health tourism is one of the oldest specific forms of tourism involving the professional and structured administration of natural healing agents and physical therapy procedures to maintain and enhance health and to improve the quality of life. Health tourism is based on the use of natural healing agents derived from the sea, thermal springs and

the climate. With the quality of modern living in steady decline due to stress and pollution, health tourism is taking on an increasingly important role in revitalising the mental and physical wellbeing of people. Health resorts provide balanced diets, exercise facilities, and social and spiritual programmes in a noise-free and pollution-free environment.

Today, health tourism products are one of the fastest growing segments of the world tourism offering. Growth is boosted not only by demographic change, but also by a universal change in social values that focus heightened attention on healthy life styles. The Kvarner region is traditionally linked to health tourism products. Owing to the region's exceptionally favourable climate and its vicinity to the then major European centres of political and economic power (Austria, Hungary, Bohemia), health tourism began to develop in the therapeutic-climate health resorts of Opatija, Crikvenica, Veli Lošinj, Rab and Gorski Kotar in the second half of the nineteenth century. At present, health reasons are a travel motivation of merely three per cent of visitors to the Kvarner region. Despite that, health tourism, in a modernised form that meets the needs of today's people, is once again a domain in which the Kvarner region intends to gain a leading position in the Adriatic. It is a key factor in creating the brand and image of a region of wellbeing, a region of "good feelings, pleasure, health, positive energy and satisfaction".

1. Health tourism in Croatia

The offering of health tourism in seaside (thalasso-therapeutic) health resorts and spa resorts is very diverse. It includes out-door activities, entertainment, wholesome activities, saunas, massages and other health-enhancing activities. The offering is based on natural healing agents that are common to a variety of medicinal, preventive and wellness programmes geared to the needs of individual groups of tourists.

In this segment of its tourism offering, Croatia provides 6,000 beds in 18 medical establishments. The number of tourists and overnights is growing by the year. According to the Central Bureau of Statistics, 27,788 tourists visited health resorts in 2010 (3.9 per cent less than in the previous year) and accounted for 331,383 overnights (three per cent less than in 2009). Out of the total number of tourists visiting Opatija in 2010 and staying for at

least one overnight, 266,630 were foreign tourists, while 64,753 were domestic tourists, representing a 3.4 per cent increase relative to 2009.

Data for the comparative year are taken from surveys in continental health resorts in which domestic tourists account for more than 90 per cent of visitors. In seaside health resorts, depending on their type, the share of foreign tourists ranges from 30 per cent to 45 per cent. According to the Central Bureau of Statistics, the average length of stay of tourists in health resorts is 14 days. In the first nine months of 2008, the number of domestic tourist arrivals to Croatian health resorts grew to 16,629, compared to 15,668 for the same period in 2007, giving an index of 106. The number of foreign tourist arrivals amounted to 13,485, making a total of 30,114 arrivals to Croatian health resorts from January to September 2008.

Previous development and estimates for the future development of health resort tourism in Croatia are based on major resources found in the diversity of the country's natural heritage, in medicinal springs, clean sea, beneficial environment and health food, and particularly in the quality of space in terms of ecology. These are also the comparative advantages Croatia has for the development of wellness tourism.

The wellness offering in Croatia is based on rich natural heritage, diverse native oils, extracts of indigenous medicinal herbs, the abundance of medicinal springs and clean sea, and extracts of marine flora, in combination with healthy, indigenous traditional food, unique aromas, and therapies inspired by exotic cultures. It has all the elements needed to create a Croatian Wellness brand for Croatia as a wellness destination.

The rising trend of tourist demand for wellness services in Croatia has resulted in an increase in wellness-service supply. This upward trend is evident in hotels that feature Hotel Wellness Centres. According to the Croatian Chamber of Economy, there were 28 Hotel Wellness Centres in late 2005; 44, in late 2006; and a total of 65, in late 2007. The number of Hotel Wellness Centres and health resorts amounted to 68 and 14, respectively, in 2010, a considerable increase in comparison with previous years.

Health tourism is about recuperating by staying in places and areas where conditions and activities exist that can help people to recover

and maintain their mental and physical abilities. This is best achieved through various therapies that are specified and administered by specialists and experts in physical and mental recreation. A tourism product for the market is designed from these therapies in combination with other tourism services.

2. Health tourism in the Kvarner region

The Kvarner is a region that is successful in capitalising on the rich history of its tourism and health-resort industry, when Opatija and Crikvenica were important health resorts of the Austro-Hungarian Monarchy.

Obviously, the situation has changed considerably since then. Today, medical facilities that have recognised and valorised Croatia's vicinity to West European countries perform well. In addition, their services are less expensive and of a far greater quality. These facilities have become the backbone of health tourism in the Kvarner region. Polyclinics providing a wide range of health care services are connecting up with hotels, restaurants and travel agencies. Of course, it would be ideal if the entire Kvarner region could become a health tourism destination with all actors engaged in its joint promotion.

It is evident in Table 1 that health reasons, as a motivation for travelling to the Kvarner destination, dropped by more than 50 per cent in 2007 in comparison with 2004.

Today's health tourism offering in the Kvarner region is heavily concentrated in three sub-regions: the Opatija Riviera, the Riviera of the Croatian Littoral, and Lošinj Island. Given the region's focus on health tourism, these sub-regions can be expected to continue to develop as Kvarner's health-tourism "specialists" in accordance with their potential. Their differentiation would be based on destination brands.

3. Health tourism products

The health tourism offering is gaining new impetus throughout the Kvarner region. The hotel wellness

offering (including the largest wellness centre on the Adriatic at Novi Vinodolski), in particular, is seeing rapid development. Parallel to this development, medical establishments of high standing, which play a vital role in creating an authentic health tourism destination, are being modernised (such as the Special Hospital Thalassotherapia, Opatija). Steps are also being taken at the destination level, foremost with regard to improvements to municipal infrastructure and the appearance of towns. Lošinj Island is an interesting example: to foster the further development of health tourism, the quality of the air – the destination's distinctive "natural healing agent" – is measured on a regular basis.

Individual health tourism products may be rated and classified into a number of categories such as wellness programmes, thalasso-therapeutic programmes and medical programmes.

Comprising some 35 wellness centres, the hotel wellness offering is the prevailing form of health tourism in the Kvarner region. Located in new or newly renovated, largely 4-star or 5-star hotels, these centres provide a high-quality (through modern equipment, trained staff, investment in the centre's ambience) internationally competitive wellness offering that includes typical services and facilities (for example, swimming pools, saunas, massages, beauty treatments, fitness facilities). Two centres that stand out are the wellness centre of the new hotel complex Novi Spa Hotels & Resort, the largest on the Adriatic coast, and that of the hotel company Liburnia Riviera Hoteli called Five Elements Wellness & Spa, a new wellness brand. Some hotel companies have opted to take over established brands and leave their management to specialists (for example, Biokozmetika manages the wellness centres at Hotel Bonavia in Rijeka and Hotel Aurora in Mali Lošinj). All hotels actively offer a variety of wellness programmes and packages. This is a well-developed health tourism product, and its further development involves introducing wellness programmes in other hotels, as well as in other types of accommodation, and fostering continuous innovation to achieve greater diversification.

Table 1: Motivations for travelling to the Kvarner region

Motivation	TOMAS Summer 2004	TOMAS Summer 2007
Passive holidaymaking, relaxation	71.1	61.9
Entertainment	30.3	59.1
New experiences	20.5	27.6
Landscapes and scenic spots	30.7	20.3
Dining experiences, gastronomy	11.1	18.1
Visits to relatives and friends	6.6	9.9
Sports and recreation	7.2	8.1
Favourable prices	7.0	7.7
Vicinity to home	10.3	6.8
Cultural sights and events	7.3	4.4
Diving	3.7	4.0
Health reasons	6.9	3.1
Shopping	0.5	2.2
Other motivations	3.8	0.9
Business	0.8	0.4
Religious reasons	0.3	0.0

Source, Institute of Tourism, Tourist Opinions and Spending in Croatia – TOMAS Summer 2007: Special Report for Primorsko-Goranska County 2008.

At present, the Thalasso Wellness Centre of Opatija is the only facility in the Kvarner region providing holiday thalasso-therapy. Set up within the framework of the Special Hospital Thalassotherapia in Opatija, this modern, top-quality centre operates separately, focusing its offering on tourists and residents. It provides typical wellness services and facilities (swimming pools, massages, beauty treatments, fitness facilities, etc.) with the distinction that all treatments and therapies are based on the use of sea water and substances derived from the sea (for example, algae, salt, sand). Treatments may be consumed individually or in theme packages. Given the current market trends and Kvarner's tradition as a (medicinal) thalasso-therapy destination, this is a health tourism product of great potential that is surely to be developed in other locations within the Kvarner region. Holiday thalasso-therapy has the potential of becoming a marker of Kvarner's health-tourism offering.

Some (smaller, private) medical establishments are promoting their services through programmes targeting tourist demand (for example, Poliklinika Terme in Selce provides wellness programmes involving a greater portion of physical therapy, as well as programmes involving diagnostics, prevention and rehabilitation). Others provide packages of specific medical services combined with tourist services and facilities (for example, dental services, minor plastic surgery, minor orthopaedic operations). This product has great potential and is in line for further development.

Certain forms of Kvarner's health tourism offering – the hotel wellness offering, in particular – are developed and well-designed products with a steady presence in the marketplace. Although less widespread, the offering of thalasso-therapeutic and medical programmes has also attained a high level of quality. Challenges facing health tourism in the Kvarner region concern the need for enterprises to continuously make innovations to the health tourism product, as well as qualitative advancements in alignment with success factors and market trends. Other challenges have emerged in the sphere of destination management, a prerequisite to improving the overall quality of health tourism products in the Kvarner region.

4. Promoting health tourism in the Kvarner region

The aim of promoting health tourism products is to establish an image of the Kvarner region as an eminent Adriatic destination of wellness, thalasso-therapeutic and medical programmes for the purpose of generating greater demand for these tourism products. Promotional activities are aimed at making the Kvarner region perceived as the best wellness and thalasso-therapy destination in the Adriatic.

The promotional mix for health tourism products is based on modern promotion methods, such as advertising, sales promotion, public relations and personal selling. The following section outlines how

promotion is carried out in the various segments of the promotional mix.

Interesting and useful information for visitors, outlining Kvarner's experience and tradition in health tourism and its high-quality, modern offering that make it the leading health-tourism destination in the Adriatic. Also, a brief description of the specific features of health-tourism sub-regions (the Opatija Riviera – broad wellness offering on a Riviera synonymous of sophistication, culture and good living; the Riviera of the Croatian Littoral – fitness programmes and the Adriatic's largest wellness centre on a riviera of energetic, athletic and youthful spirit; Lošinj Island – wellness and vitality in an entirely natural way in an extraordinarily clean environment). An outline of the major forms of Kvarner's health-tourism offering: wellness, thalasso-therapeutic and medical programmes. A description of healthy living in the Kvarner region (for example, typical healthy Mediterranean diet, numerous opportunities for walking, hiking and sports activities, etc.).

Printed materials focus on depicting the pleasure and satisfaction derived from a health-tourism vacation in a region leading in this type of offering.

Brand image elements in brochures include a narrative the Kvarner region's tradition and expertise in health tourism, focusing on the quality of the environment and presenting the region's offering of wellness, thalasso-therapeutic and medical programmes and the specific traits of leading destinations. By outlining opportunities for enjoying recreational activities, gastronomy, culture, excursions and tours, brochures present the Kvarner region as an appealing destination providing a fulfilling experience. Information-providing elements include a comparative presentation of the health tourism offering of destinations and centres, facts on the quality of natural healing agents (climate, air, sea), an overview of accommodation opportunities, and useful information about reaching and staying in the destination (for example, what to see and experience, what to try, etc.)

Public relations are based on thematic newsletters and New Media targeting guests, (specialised) journalists and intermediaries, and carrying news and "stories" about Kvarner's health tourism offering. A variety of study tours are organised, as well as study tours for (specialised) journalists and

intermediaries. Study tours are designed to acquaint participants with the health tourism offering of the Kvarner region by centring on its long tradition in and current focus on health tourism products, its expertise, the special features of thalasso-therapy, its imposing wellness offering including several brands, and its high-quality offering of medical programmes.

Drawing attention to the specific features of leading destinations (the fashionable Opatija Riviera, the sports-oriented Riviera of the Croatian Littoral, natural and wholesome Lošinj Island). Attention is also focused on issues concerning the environment and professional staff. The region's gastronomic, recreational and cultural offerings are highlighted. Trips with a theme-based itinerary can be organised.

Workshops, business workshops for tourism professionals and (specialised) intermediaries presenting health-tourism vacations in the Kvarner region. Focus is placed on long tradition, the special features of thalasso-therapy, the imposing wellness offering with several brands, high-quality medical programmes, and leading destinations within the region. Attention is also drawn to the quality of natural healing agents and professional staff. Workshops may include special themes (for example, the benefits of thalasso-therapy, the local natural ingredients used in wellness treatments, etc.) or the local health food offering. Specialised trade shows, participation in specialised trade shows for health, wellness and beauty. Focus on the thalasso-therapy offering and expertise, imposing and partially branded wellness offering, and the high quality of the medical-programme offering.

Special presentations, as part of general and/or specialised trade shows, featuring the Kvarner region as a top-quality health-tourism destination providing a comprehensive tourist experience. Guests at these presentations may be professionals from various wellness centres or thalasso-therapy centres. Treatments may be demonstrated "live". The offering of local organic products and gastronomy may also be demonstrated.

Advertisements, the final element of the promotional mix, are placed in the sales catalogues and/or internal journals of specialised intermediaries, as well as selected journals according to the media plan. Advertisements focus on the region's expertise, on wellbeing and comfort, presenting

Kvarner as the best place for a wellness and thalasso-therapy vacation in the Adriatic.

5. Thalassotherapy and Thalasso Wellness Centre, Opatija

Recent years have seen the steady development of a new form of health tourism, located primarily in hotel facilities, but also in specialised establishments that combine the elements of medicine and tourism.

One such establishment is Thalassoterapia Opatija, a specialised hospital for medical rehabilitation and the treatment of cardiopathy, lung diseases and rheumatism. Initially founded in 1957 as the Institute of Thalassotherapy following a century-old tradition of health tourism, today it is the region's leading centre for cardiological rehabilitation and one of its largest non-invasive cardiac diagnostics laboratories. Since its beginnings, Thalassoterapia Opatija has focused its services on both the domestic and the foreign market. The centre's clients are especially interested in physical therapy and anti-rheumatism programmes, preventive cardiac programmes, as well as nutrition care programmes, sports programmes and dermatology programmes.

In health tourism, prices need to be competitive; the quality of services, beyond reproach and standardised; and services, designed as packages in a way that is not available to clients at their place of residence.

Today thalasso-therapy establishments catering to tourists provide services and treatments under the care of specialist doctors. Treatments include exercise, relaxation, underwater exercise, kinesis therapy, programmes for alleviating insomnia, smoking cessation programmes, slimming programmes, beauty treatments, and other treatments aimed at relieving or curing a variety of infirmities and discomforts in the time tourists have set aside for vacation.

Peak months at the Thalasso Wellness Centre last from October to May. Foreign guests mostly use the Centre's services during the summer months or during holidays. The most frequent guests are Italians, Russians and Slovenes, and Germans, to a smaller extent. The Centre has signed a

Cooperation Agreement with Vienna International Hotels, a group that manages the hotels Astoria, Bristol and Opatija in Opatija. It also collaborates with several foreign and domestic travel agencies. In addition to offering the Centre's services, these agencies also provide accommodation in Villa Magnolia, boasting seven highly standardised and medically equipped double rooms; in Villa Dubrava, with 36 rooms and some 65 beds; or in other hotels.

Table 2 shows the number of clients using the services of Thalasso Wellness Centre in 2010. Foreign clients and domestic clients accounted for 70 per cent and 30 per cent, respectively, of the total number of clients. The table attests to the Centre's year-round operations. The Centre's data also indicate client numbers are growing by the year.

This increase in client numbers is the result of the successful implementation of a promotional mix targeting, and creating offerings for, guests belonging to the mature age group (50 – 65) and young couples (25 – 35). Other target groups include single-day visitors and domestic visitors in the Kvarner region.

For the most part, the Centre's promotional activities are focused on printed material and the Internet. The tradition of thalasso-therapy in the Kvarner region is outlined, highlighting the purity of the environment and the sea, the healthy climate, and the quality of natural healing agents. Promotional materials also present the thalasso wellness offering, underlining its quality and the moods and experiences provided by the offering's various segments. Their design places them in the category of promotional leaflets promoting the Kvarner's tourism products.

Conclusion

The conclusion derived from this paper is that the health offering is insufficiently valorised in Croatia's tourism industry. It is essential for Croatian tourism to understand that health-related services and facilities are a component part of the tourism offering. In this way, the tourism industry is given new tasks, tasks that are not only socially worthy and beneficial, but also provide new opportunities for socioeconomic development.

Table 2: Number of Thalasso Wellness Centre clients in 2010

	Number of clients
January	2344
February	2743
March	2661
April	2706
May	2398
June	1645
July	892
August	1275
September	1738
October	1874
November	2878
December	2855
TOTAL	26,009

Source: Thalassotherapie and Thalasso Wellness Centre Opatija, Marketing Dept.

Considering the general trends shaping the “new tourist”, the specific trends and success factors of the health tourism product, and the attributes of major target segments of customers, health tourism can be said to be a young branch relying the successfulness of promotion.

Results achieved in the health tourism segment indicate that the promotion of the Kvarner region has been exceptionally successful in recent years. Building on its longstanding tradition as a health resort, Thalassotherapie and Thalasso Wellness Centre Opatija have achieved year-round occupancy, thus improving the situation of health tourism in the Kvarner region.

The success of the current promotional activity of Thalassotherapie and Thalasso Wellness Centre Opatija is reflected in the number of its clients and visitors. Nevertheless, efforts are needed to expand the promotional mix by making certain events a tradition (such as, special offers for various months of the year), and participating in a greater number of trade shows and medical conferences with an offering containing new services and facilities and

customised to the needs of various age groups and the preferences of individuals.

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SOURCES OF SHORT-TERM FINANCING

ELEONORA KONTUŠ
THE TOWN OF KASTAV, CROATIA

Abstract

The aim of the paper is, first of all, to analyze various sources of short-term financing, secondly, to explore procedures to convert different terms and conditions for various types of short-term financing sources into effective interest rates after tax and, thirdly, to establish the relationship between a set of independent variables in order to produce an effective interest rate after tax as a dependent variable. To determine what sources of short-term financing to employ, it is important to take into consideration the cost of all available sources expressed as a comparable effective interest rate after tax and choose the source in accordance with the effective interest rate after tax because that represents the real cost of financing. Finally, the source that has the lowest effective interest rate after tax should be chosen. The results of the work will provide equations for calculating effective interest rates after tax for different short-term financing sources e.g: line of credit, simple interest bank loans, bank loans with discount interest, bank loans with compensating balances, bank loans with discount interest and compensating balances, secured bank loans, instalment loans, factoring accounts receivable and commercial papers. On the basis of the above, it can be determined that an effective interest rate after tax can be accurately calculated using these equations. The results lead to the conclusion that consideration and comparison of all available sources regarding costs are easier as calculation of an effective interest rate is simplified by using the given equations.

Key words: sources of short-term financing, cost of sources, effective interest rate after tax, equations for calculating effective interest rate

Introduction

Sources of short-term financing can be defined as any liability originally scheduled for payment

within one year and can be characterized by cost, availability, degree of management discretion allowed and security required. Costs are the most important factor and financial managers have to minimize these. The Effective Interest Rate After Tax (EIRAT) is a true measure of the effective cost of sources of short-term financing. It is important to calculate EIRAT for each type of short-term fund source before deciding on which type to be used and the financing source that has the lowest EIRAT should be chosen. The finance manager should select the least expensive alternative.

The purpose of this study is to determine how to make optimum use of available short-term financing sources from a cost perspective. In striving to fill in the gaps relating to EIRAT as a real cost of short-term financing, the study makes its own contribution to research and thereby to managers. With the aim of completing these gaps, the study will investigate various sources of short-term financing and explore what key factors influence EIRAT.

The outcome is not only to define variables important to EIRAT and establish functional correlations between variables in order to yield EIRAT, but also to demonstrate an awareness of the causal relationship and give general recommendations for financial managers.

Theoretical background

Business borrows short term for seasonal working capital, to cover abrupt changes in payment patterns or unexpected expenses, and when short-term profitability is not adequate to support continued operations. Sources of short-term financing can be spontaneous or negotiated financing sources. A spontaneous source of financing is one that occurs automatically as a result of operations (Maness and Zietlow, 2005). Common spontaneous sources are payables and accruals. Accounts payable is a spontaneous financing source since it comes from

normal business operations. A company having liquidity problems may stretch its accounts payable, but the disadvantage of doing so are the giving up of any cash discount offered and the probability of lowering the firm's credit rating. An accrual is an expense that has been incurred but has not yet been paid as accrued wages and accrued taxes. Accruals represent a spontaneous source of financing in that as the business expands, the level of operations expands, as does the level of accrued wages and taxes.

Bank loans are an important source of short-term credit. Interest on bank loans may be quoted as simple interest, discount interest or installment interest. Bank loans can be single-payment loans and installment loans. A single-payment loan is paid in full on a given date. There are two ways of calculating interest on single-payment loans: the simple interest method and the discount method. The difference between the two is in the amount the borrower actually receives. Under the simple interest method, interest is calculated only on the amount borrowed. With discount interest, the interest is deducted from the amount of the loan at the beginning, thereby reducing the net amount of the financing obtained. An installment loan requires monthly payments. Instead of paying the loan off in a lump sum banks charge installment interest, with payments made monthly. In this case the total amount of interest is calculated and added to the original face value of the note. Then the monthly installment represents a payment of both principal and interest. The cost of installment loan is always higher than the stated nominal rate (Pinches, 1994).

When a loan has a compensating balance requirements associated with it, the proceeds received by the borrower are decreased by the amount of the balance.

Bank financing may take any of the following forms: lines of credit, unsecured loans and secured loans. Under a line of credit, the bank agrees to lend money to the borrower on a recurring basis up to a specified amount. The advantages of a line of credit for a company are the easy and immediate access to funds during tight money market conditions and the ability to borrow only as much as needed and repay immediately when cash is available. The bank charges a commitment fee on the amount of the unused credit line and an interest on the amount of the used credit line. Unsecured loan is recommended for use by companies with excellent

credit ratings for financing projects that have quick cash flows. The disadvantages of this kind of loan are that, because it is made for the short term, it carries a higher interest rate than a secured loan and payment in a lump sum is required. Secured loan is loan on a secured basis, with some form of collateral behind the loan. Collateral may take many forms including inventory, accounts receivable or securities. Even though the company is able to obtain an unsecured loan, it may still give collateral in exchange for a lowest interest rate.

Commercial paper is unsecured short-term debt issued by a large, financially strong corporation. Although the cost of commercial paper is lower than the cost of bank loans, commercial paper's maturity is limited to 270 days, and it can be used only by large firms with exceptionally strong credit ratings (Brigham and Gapenski, 1997). The interest rate is less than that of a bank loan and it can be issued only by companies possessing the highest credit ratings. The yields on commercial paper are generally less than the effective cost of bank lines of credit, which explains why banks have lost a portion of its short-term lending to those firms that can access the commercial paper market (Maness and Zietlow, 2005).

Factoring receivables involves the purchase of accounts receivable by the lender. The receivables may be sold «without recourse». In such a case the factor makes the credit-granting decision and incurs any losses from nonpayment by the firm's customers. Under recourse factoring, the granting firm typically makes the credit-granting decision and, therefore, bears the consequences of any nonpayment by the customers. Factoring operates in two basic ways. The first is maturity factoring, in which the factor purchases all receivables and once a month pays the seller for the receivables. The second factoring method is advance factoring, in which the factor provides a loan against the receivables (Pinches, 1994).

Inventory financing is an extremely critical component of the total financial plan of most corporations. This is because inventory has generally represented a significant portion of the corporation's total working capital, and inventory represents a resource commitment which has yet to release cash and will not do so until the item is sold and cash collected (Maness and Zietlow, 2005). A substantial amount of credit is secured by business inventories. There are three primary methods of inventory financing: an inventory

blanket lien, a trust receipt and warehouse receipt financing.

The merits of the different alternative sources of short-term financing should be considered carefully before a company borrows money. The factors bearing upon the selection of the source of short-term financing include: cost, effect on credit rating, risk, restrictions, flexibility, expected money market conditions, the inflation rate, corporate profitability and liquidity positions and the stability of company's operations (Shim and Siegel, 2007).

The cost of short-term financing sources is the most important factor. The effective interest rate is the real rate of interest on a loan, expressed as an annual percentage applicable for the life of the loan. Short-term financing arrangements have several features that cause the stated interest rate on the financing to be different from the effective interest rate. A discounted loan and a compensating balance increase the effective interest rate. The tax paid by a company triggers a decrease of the effective cost of short-term financing and the Effective Interest Rate After Tax (EIRAT) represents the real cost of financing. Sources of short-term financing have been explored and discussions about calculating the effective interest rate on some forms of short-term financing have been made but there are still gaps relating to EIRAT in the existing literature.

Research

Methodology

An Effective Interest Rate After Tax (EIRAT) can be calculated by applying procedures for computing this. In this research, it is essential to determine independent variables which impact on EIRAT as dependent variables and to establish their relation to these independent variables. The applied procedures for calculating EIRAT for various short-term financing sources are

considered suitable in determining independent variables; these in turn are deemed significant for EIRAT and this should be expressed in terms of these independent variables. The process of calculating EIRAT is shown and can be reduced to that of finding deterministic functions and solving equations which take these into account.

Models have been designed on the basis of the results of analysis of these procedures. The first step in designing a model is to define the objective of the model. The next step is to specify the independent variables to be used in the model. The third step in the modelling process is to determine the relationship between the selected independent variables so that EIRAT can be computed. All independent variables that appear at every stage of calculating EIRAT and their impact on EIRAT have been considered. Finally, the independent variables which determine EIRAT for all short-term financing sources have been selected and the relations between them have been defined. For precise formulation of the relationship between a set of independent variables, mathematical methods have been adapted in order to yield EIRAT as a dependent variable.

Results of analysis

The procedures used to convert different terms and conditions for various types of short-term financing sources into a comparable EIRAT are explained and analyzed, focusing on independent variables which impact on EIRAT. We have analyzed the following financing sources: line of credit, simple interest bank loans, bank loans with discount interest, bank loans with compensating balances, bank loans with discount interest and compensating balances, secured bank loans, installment loans, factoring accounts receivable and commercial papers.

Line of credit

We employ the following steps to determine EIRAT for 1-year credit line:

- Calculation of a commitment fee for unused period

$$\text{Commitment fee} = \frac{\text{principal} \times \text{commitment fee (\%)} \times \text{unused period}}{1200}$$

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)} \times \text{used period}}{1200}$$

- Calculation of total credit line cost

$$\text{Total cost} = \text{interest} + \text{commitment fee}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{total cost}}{\text{principal}} \times 100$$

- Tax savings from total cost

$$\text{Tax savings} = \frac{\text{total cost} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{principal}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate, commitment fee (%), used period and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \frac{\text{nominal interest rate (k)} \times n + \text{commitment fee (\%)} \times (2 - n)}{2} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

n – used period expressed in months.

Simple interest bank loan

The procedure used to calculate an Effective Interest Rate After Tax (EIRAT) for simple interest bank loans includes the following steps:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{principal}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{principal}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate and profit tax rate. The principal is labeled as not relevant variable for EIRAT and is excluded. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \text{nominal interest rate (k)} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent.

Bank loan with discount interest

The process of calculating EIRAT for bank loans with discount interest involves the following calculations:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate } (k)}{100}$$

- Calculation of real used amount of bank loan

$$\text{Proceeds} = \text{principal} - \text{interest}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{proceeds}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate } (\%)}{100}$$

- Percentage of tax savings

$$\text{Tax savings } (\%) = \frac{\text{tax savings}}{\text{proceeds}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings } (\%)$$

The independent variables which have an impact on EIRAT are nominal interest rate and profit tax rate. EIRAT can be expressed in terms of these independent variables as follow:

$$\text{EIRAT} = \frac{\text{nominal interest rate } (k)}{100 - \text{nominal interest rate } (k)} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent.

Simple interest bank loan with compensating balances

The procedure for computing EIRAT for simple interest bank loans with compensating balances includes the following steps:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of compensating balances

$$\text{Compensating balances} = \frac{\text{principal} \times \text{compensating balances (\%)}}{100}$$

- Calculation of real used amount of bank loan

$$\text{Proceeds} = \text{principal} - \text{compensating balances}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{proceeds}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{proceeds}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate, compensating balances (%) and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$EIRAT = \frac{\text{nominal interest rate } (k)}{100 - \text{compensating balances } (\%)} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent.

Bank loan with discount interest and compensating balances

The analyses can be extended to the case where compensating balances are required and the loan is on a discount basis. In this situation the procedure for calculating EIRAT includes the following steps:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate } (k)}{100}$$

- Calculation of compensating balances

$$\text{Compensating balances} = \frac{\text{principal} \times \text{compensating balances } (\%)}{100}$$

- Calculation of real used amount of bank loan

$$\text{Proceeds} = \text{principal} - \text{interest} - \text{compensating balances}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{proceeds}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate } (\%)}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{proceeds}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate, compensating balances (%) and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \frac{\text{nominal interest rate (k)}}{100 - \text{nominal interest rate (k)} - \text{compensating balances (\%)}} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent.

Installment loan

The procedure for computing an Effective Interest Rate After Tax (EIRAT) of an installment loan includes the following steps:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of real used amount of loan

$$\text{Proceeds} = (\text{principal} + \text{principal} / 2) / 2$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{proceeds}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{proceeds}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate and profit tax rate. The relationship between these independent variables in order to produce EIRAT can be defined mathematically as:

$$\text{EIRAT} = \frac{\text{nominal interest rate (k)} \times 2}{(1 + 1/12)} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent.

Secured bank loans

The procedure used to calculate EIRAT for secured bank loans on the basis of one collateral involves the following calculations:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{principal}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{principal}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \text{nominal interest rate (k)} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent.

The calculations required to determine EIRAT for secured bank loans on the basis of two collaterals are slightly more complicated and the following process must be adhered to:

- Calculation of total interest cost of both loans

$$\text{Total interest} = \frac{\text{principal (1)} \times \text{nominal rate (k)} + \text{principal (2)} \times \text{nominal rate (k)}}{100}$$

- Calculation of total amount of loans

$$\text{Total amount of loans} = \text{principal (1)} + \text{principal (2)}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{total interest}}{\text{total amount of loans}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{total interest} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{total amount of loans}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are the principals of both loans, nominal interest rates of both loans and profit tax rate. The relationship between these independent variables in order to produce EIRAT can be defined mathematically as:

$$\text{EIRAT} = \frac{\text{principal (1)} \times \text{nominal rate (k}_1) + \text{principal (2)} \times \text{nominal rate (k}_2)}{\text{principal (1)} + \text{principal (2)}} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k₁, k₂ – nominal interest rates expressed as percents.

Factoring accounts receivable

The process of calculating EIRAT for factoring accounts receivable involves the following calculations:

- Calculation of a factor fee

$$\text{Factor fee} = \frac{\text{receivables purchases} \times \text{factor fee (\%)}}{100}$$

- Calculation of cost of borrowing deducted in advance

$$\text{Interest} = \frac{\text{receivables purchases} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of real used amount

$$\text{Proceeds} = \text{receivables purchases} - \text{interest} - \text{factor fee}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{interest}}{\text{proceeds}} \times 100$$

- Tax savings from interest cost

$$\text{Tax savings} = \frac{\text{interest} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{proceeds}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have an impact on EIRAT are nominal interest rate, factor fee (%) and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \frac{\text{nominal interest rate (k)}}{100 - \text{nominal interest rate (k)} - \text{factor fee (\%)}} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent

f – factor fee expressed as percent.

Inventory financing

The process of calculating EIRAT for inventory financing includes the following calculations:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of total cost

$$\text{Total cost} = \text{interest} + \text{warehousing cost}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{total cost}}{\text{principal}} \times 100$$

- Tax savings from total cost

$$\text{Tax savings} = \frac{\text{total cost} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{principal}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have impact on EIRAT are nominal interest rate, warehousing cost and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \left(\underset{\text{where}}{\text{nominal interest rate (k)}} + \frac{100 \times \text{warehousing cost}}{\text{principal}} \right) \times (1 - p)$$

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent.

Commercial papers

The procedure for computing an Effective Interest Rate After Tax (EIRAT) for issuance of commercial papers includes the following steps:

- Calculation of interest cost

$$\text{Interest} = \frac{\text{principal} \times \text{nominal interest rate (k)}}{100}$$

- Calculation of total cost

$$\text{Total cost} = \text{interest} + \text{cost of issuance of commercial paper}$$

- Calculation of an effective interest rate

$$\text{Effective interest rate} = \frac{\text{total cost}}{\text{principal}} \times 100$$

- Tax savings from total cost

$$\text{Tax savings} = \frac{\text{total cost} \times \text{profit tax rate (\%)}}{100}$$

- Percentage of tax savings

$$\text{Tax savings (\%)} = \frac{\text{tax savings}}{\text{principal}} \times 100$$

- Calculation of an effective interest rate after tax

$$\text{EIRAT} = \text{effective interest rate} - \text{tax savings (\%)}$$

The independent variables which have impact on EIRAT are nominal interest rate, cost of issuance and profit tax rate. EIRAT can be expressed in terms of these independent variables as follows:

$$\text{EIRAT} = \left(\text{nominal interest rate (k)} + \frac{100 \times \text{cost of issuance}}{\text{principal}} \right) \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent.

Discussion

This research shows that a wide range of factors affect the Effective Interest Rate After Tax (EIRAT) for short-term financing sources. For all these sources, EIRAT is a function of a nominal interest rate and a profit tax rate. An upsurge in the nominal interest rate produces an increase in terms of EIRAT, while a rise in the profit tax rate triggers a decrease of EIRAT.

Other factors that influence EIRAT are:

- compensating balance
- a method for calculating interest
- cost of issuing commercial papers
- warehousing costs
- factor fee
- as well as commitment fee.

A compensating balance increases EIRAT. The methods for computing interest costs, such as the discount and installment method, also increase EIRAT.

This subsequently rises, as the cost of issuing commercial papers or warehousing costs escalate accordingly. A hike in the factor or commitment fee also produces an upsurge in terms of EIRAT.

The independent variables over which management can exert some degree of control are a nominal interest rate, compensating balance, cost of issuing commercial papers, warehousing costs, factor fee and commitment fee, while profit tax rate is the variable which manager should take as

given. A manager can also impact on the method of calculating interest which will be used.

The findings of this research show that the following general recommendations for financial managers have been compiled on the basis of this research. Financial managers should impact on the independent variables over which they have some degree of control in order to reduce them. They should obtain bank loans without compensating balance and arrange payment of interest costs on the real used amount of a bank loan because compensating balance, discount interest and installment interest raise EIRAT on bank loans.

Financial managers have a wide assortment of bank or nonbank short-term financing sources from which to choose. To determine what sources of short-term financing to employ, managers should take into consideration the cost of all available sources expressed as a comparable EIRAT and choose the source in accordance with EIRAT because that represents the real cost of financing. Finally, the source that has the lowest EIRAT should be chosen.

Models

To enable us to model the relations between independent variables which determine an Effective Interest Rate After Tax (EIRAT) as a dependent variable, new equations have been introduced.

Consequently, the main findings are new equations for calculating EIRAT for all short-term financing sources:

Line of credit

$$EIRAT = \frac{\text{nominal interest rate } (k) \times n + \text{commitment fee } (\%) \times (2 - n)}{2} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

n – used period expressed in months

Simple interest bank loan

$$EIRAT = \text{nominal interest rate } (k) \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

Bank loan with discount interest

$$EIRAT = \frac{\text{nominal interest rate } (k)}{100 - \text{nominal interest rate } (k)} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent

Simple interest bank loan with compensating balances

$$EIRAT = \frac{\text{nominal interest rate } (k)}{100 - \text{compensating balances } (\%)} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent

 Bank loan with discount interest and compensating balances

$$EIRAT = \frac{\textit{nominal interest rate (k)}}{100 - \textit{nominal interest rate (k)} - \textit{compensating balances (\%)}} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent

Installment loan

$$EIRAT = \frac{\textit{nominal interest rate (k)} \times 2}{(1 + 1/12)} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

Secured bank loans on the basis of one collateral

$$EIRAT = \textit{nominal interest rate (k)} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

Secured bank loans on the basis of two collaterals

$$EIRAT = \frac{\textit{principal (1)} \times \textit{nominal rate (k}_1) + \textit{principal (2)} \times \textit{nominal rate (k}_2)}{\textit{principal (1)} + \textit{principal (2)}} \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k₁, k₂ – nominal interest rates expressed as percents

Factoring accounts receivable

$$EIRAT = \frac{\text{nominal interest rate } (k)}{100 - \text{nominal interest rate } (k) - \text{factor fee } (\%)} \times (100 - p)$$

where

p - profit tax rate expressed as percent

k – nominal interest rate expressed as percent

f – factor fee expressed as percent

Inventory financing

$$EIRAT = \left(\text{nominal interest rate } (k) + \frac{100 \times \text{warehousing cost}}{\text{principal}} \right) \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

Commercial papers

$$EIRAT = \left(\text{nominal interest rate } (k) + \frac{100 \times \text{cost of issuance}}{\text{principal}} \right) \times (1 - p)$$

where

p - profit tax rate expressed as decimals

k – nominal interest rate expressed as percent

Benefits that can be derived from these equation models include the following:

- Calculation of EIRAT is simplified.
- Consideration and comparison of all available sources regarding costs are easier as calculation of EIRAT is simplified by using the given equations.
- The best selection of short-term financing sources can be made.
- The ability to explore more alternatives is given by using these equations.
- More accurate forecasts are made.
- Significant cost savings can be achieved by taking into consideration the cost of all available sources.
- Better quality and faster short-term financial decisions can be made.

Conclusion

An Effective Interest Rate After Tax (EIRAT) represents the real cost of financing and to determine what sources of short-term financing to employ it is important to take into consideration the cost of all available sources and choose the source in accordance with EIRAT. The development of the models essentially involves definition of variables and model specification.

We have analyzed procedures for calculating EIRAT for all short-term financing sources in order to define independent variables which determine EIRAT and investigate if there is a possible correlation between them. Models have been designed on the basis of the results of analysis.

Major findings are new equation models for calculating EIRAT for all short-term financing sources e.g: line of credit, simple interest bank loans, bank loans with discount interest, bank loans with compensating balances, bank loans with discount interest and compensating balances, secured bank loans, installment loans, factoring accounts receivable and commercial papers. EIRAT can be accurately calculated using these equations.

The contribution of this paper is to model all the relationships between independent variables which determine EIRAT for all short-term financing sources as dependent variables. The equation models can be used as a tool to help minimize costs and develop the optimal composition of the company's short-term liabilities in the aspect of economy.

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RISK OF STRUCTURING: MEASUREMENT POTENTIAL OF DIFFERENT MODELS

BARBARA DÖMÖTÖR
CORVINUS UNIVERSITY OF BUDAPEST, HUNGARY

Abstract

The increased volatility and the weakening of the Hungarian forint during the recent financial crises caused huge financial losses for several corporations (exporters). Although all the short foreign-exchange positions in euro suffered from the market movements, the more complicated structures got in the focus of attention, since most of them were thought to be a hedging deal, thereby free of any risk. In this paper, I examine the risk of a special foreign exchange derivative, spread on the Hungarian market before the crisis. The risk measures are calculated using three methods: the historical simulation, simulation based on a simple model of geometric Brownian motion and a GARCH-model. I compare the riskiness of the product forecasted by these methods in the autumn 2008, at the time preceding the eruption of the crisis in Hungary. I investigate whether the risk of huge potential losses could have been foreseen at least by the distributing banks, and to what extent were the more sophisticated risk measure tools able to forecast the potential negative outcome. Based on the results, all the three models give warning signals as to the scale of the risk taken with high Value-at-Risk and expected shortfall figures, but the decision making was dominated by the low probability of the negative outcomes. The Cash-flow at Risk analysis presents, that albeit the product is not an appropriate hedging device, it caused financial difficulties mainly for speculators.

Keywords: foreign-exchange risk, exchange rate modelling, value-at risk, structured derivatives

Introduction

The Hungarian forint (HUF) – after some years of pegging to the euro - is a free-floating currency

that is traded in the interbank market against the euro (EUR) principally. Being a European Union member state, Hungary transacts its international trade mainly with EU countries. Consequently the major foreign exchange exposure of Hungarian corporations is generated in EUR/HUF terms. Before the crisis reached Hungary in 2008, the exchange rate movement of the currency-pair was very stable. Despite of the massive swap-difference caused by the relative high forint yields, the forint did not weaken, but rather strengthened against the common currency. Figure 1 shows the exchange rate movement of the pre-crisis period: the exchange rate moved in a narrow range around the level of 250 EUR/HUF. Each increase of the exchange rate was followed by a fast consolidation that ensured a mean reverting characteristic to the EUR/HUF rate. Therefore, market participants stood in one direction: they shorted the euro for hedging purposes and for speculation as well.

The financial innovation during the decade aimed at using the high yield difference combined with the stability of the forint by developing complex currency products both for hedgers and speculators. These structures offered better than market prices, but contained some obligations in form of short options, or early termination of the deal. During the peaceful years, investors enjoyed the advantages of these structures, and forgot all about the costs, namely the risks incurred. After the eruption of the financial crisis in the autumn of 2008, the euro short positions were hit from three sides: not only the exchange rate rose to a level never seen before, but both the forint yields and volatility increased. The severe losses of the most complicated products got in the spotlight, questioning the rationality of structuring.

Figure 1 - EUR/HUF daily ECB fixings 2002-2008

Source: ECB statistics

Table 1 - Parameters of the profitmax forward agreement as of the 7th of October 2008.

Notional value at each expiry	100,000 EUR
Currency to be sold	EUR
Currency to be bought	HUF
Expiries	1-12 month
Spot rate	250.00
Profitmax forward rate	265.00
Maximum profit	3,000,000 HUF

Source: K&H handbook

The subject of this paper is an example on the described financial engineering: the profitmax forward agreement, offered primarily to exporters, to "hedge" their foreign currency denominated income. I investigate the risk quantified by some risk measures, anticipated just before the market fall in 2008.

The next section introduces the analysed structure called the profitmax forward agreement, and then the three exchange rate models, used in the

simulation are described. The second part of the paper contains the results of the analysis from two aspects: the riskiness of the product by itself, and as a hedging device.

profitmax forward agreements

The structure consists of a series of EUR/HUF conversions on given future dates at a price higher than the market forward price, but the profit achieved on the conversions is maximised by a predetermined amount. The profit is calculated as the cumulated amount of the positive differences between the profitmax forward rate and the actual spot rate at expiry (measured by the daily fixing of the European Central Bank), multiplied by the notional value, without compounding. In case the profit cap is reached, further legs cease to exist. Although marketed for exporters, the structure is not to serve hedging purposes, because the protection against the falling exchange rate is limited: the structure is not able to grant a worst-case rate for the whole exposure of the would-be hedger. The payout feature of the profitmax is close to a short option position, since there is a high chance for a limited profit, but the loss potential of the deal is infinite.

The parameters of the profitmax agreement to be analysed are shown in table 1. The structure consists of 12 conditional exchanges of 100,000 euro to Hungarian forint at an exchange rate of 265.00 EUR/HUF. The profitmax forward rate is much higher (8.50 forint) than the market rate of a cross-currency swap allowing the conversions of the same amounts at the same maturities. The cost of the more favourable exchange rate is the possibility of termination.

The profitmax structure appeared in the market in the middle of this decade, and due to the stable market movements the first deals expired in 2-4 month realizing the maximum profit. Both the financial institutions and their clients were satisfied, and the product started to be marketed for a wider range of the customers. The profit of the upside was clear, but the potential loss was regarded negligible, even in the banking communication. After the market turndown the dark-side of the structure came to the light, the higher spot and swap-rates caused huge realized or non-realized losses on the shorted euro positions. Table 2 contains the reference rates in fact at the expiry dates of the profitmax forward agreement

concluded on the 7th of October 2008. According to these rates, the realized loss amounted more than 19.6 million forint calculated for the last expiry date of 7th of October 2009 (using forint interbank rates for compounding).

Holders of such products were shocked by realizing so large losses on their position that they previously conceive as quasi risk-free. In the following sections, I analyse whether the suffered losses could have been foreseen, and to what extent is the communication or the risk management to be blamed for the incomprehension from the side of the clients.

Exchange rate models

In order to analyse the riskiness of the structure, the future exchange rate (ST) movement is to be modelled. As generally accepted in the financial literature, the logarithm of the chain-indices of the daily exchange rates, the logarithmic return (y_t) is modelled.

$$y_t = \ln(S_t / S_{t-1}) \quad (1)$$

$$S_T = S_0 e^{\sum_{t=1}^T y_t} \quad (2)$$

Monte Carlo simulation was applied, according to three methods, to generate future daily returns, based on them 1,000 future exchange rate trajectories were simulated in Matlab and MS Excel. All three methods require a representative reference period from the past, based on which the daily market changes of the following 1-year period are simulated. The chosen reference period has a fundamental impact on results, therefore it is to be determined long enough to be representative, but not too long to remain relevant. On the other hand, none of these methods are able to predict structural changes in the time series. By considering all the above described aspects, I took the previous five years as a reference period (from October 2003 up to October 2008).

Table 2 - EUR/HUF ECB fixing rates at the exchange dates

Date	EUR/HUF
2008.11.07	269.00
2008.12.05	265.32
2009.01.09	276.13
2009.02.06	292.60
2009.03.06	316.50
2009.04.07	296.80
2009.05.08	277.75
2009.06.08	287.19
2009.07.07	273.20
2009.08.07	272.80
2009.09.07	272.24
2009.10.07	267.90

Source: ECB statistics

Historical simulation

The method assumes that market movements of the past are representative for the future. In this context, a random choice from the daily logreturns of the past reference period is an appropriate proxy for the future. The advantage of the method is that no assumption about the future distribution of the price changes is needed, and it handles also the fat tail phenomenon: frequency of the extreme values, which is essential from the aspect of risk management.

Simulation with geometric Brownian motion (GBM)

The random characteristic of the traded assets was discovered at the beginning of the 20th century (Bachelier 1900), and the Brownian motion used in physics to describe the movements of molecules was applied for the logarithmic change of financial asset prices (Osborne 1959). According to the discrete version of the model, the logreturn of a period Δt consists of a deterministic and a stochastic part:

$$y_t = m\Delta t + \varepsilon \sqrt{\Delta t} \quad (3)$$

where ε is a standard normally distributed stochastic variable, m and σ are positive constants.

The parameters – the drift (m) and the volatility (σ) – are estimated from the average and the standard deviation of the daily logreturns of the reference period. Using the daily price changes between October 2003 and 2008 the equation is the following:

$$y_t = -0.0096\Delta t + 0.0783\varepsilon\sqrt{\Delta t} \quad (4)$$

Simulation with GARCH(1,1) model

Some stylized facts of the financial time-series, like the higher probability of extreme values (fat tail phenomenon) or the serial correlation of volatility (volatility clustering) could not be explained in the traditional model framework. Based on the work of Engle (1982), which releases the assumption of constant variance of the time series and allows a conditional variance depending on the errors of the past, Bollerslev (1986) developed the

model of Generalized Autoregressive Conditional Heteroskedasticity by building the lagged conditional variances into the model as well. A GARCH model is commonly used for FX rates prediction. The expected value (5) and variance equations (6) of the GARCH(1,1) model are:

$$y_t = c + e_t = c + s_t Z_t \quad (5)$$

$$s_t^2 = a_0 + a_1 e_{t-1}^2 + b_1 s_{t-1}^2 \quad (6)$$

Where y_t denotes the logarithmic returns, σ_t stands for the standard deviation and Z_t is an independent standard normal distributed random variable. I fit GARCH(1,1) to the above 5-year panel of the logarithmic returns, the parameters are estimated by the maximum likelihood method. Table 3 contains the parameters of the model.

The constant of the expected value equation proved to be insignificant, but all the parameters of the variance equation have low p-values, the sum of the a_1 and b_1 parameters is high, showing the long persistence of the shocks, but below one, ensuring a finite unconditional variance. The GARCH(1,1) model used to the simulation of the logarithmic return is:

$$y_t = e_t = s_t Z_t \quad (7)$$

(8)

The starting spot rate was 250 EUR/HUF, and were taken to be zero and the unconditional variance respectively.

Results of the Value-at Risk type analysis

The distribution of the future value of the profit on the last expiry (7th October 2009) of the profitmax forward agreement (parameters according to table 1) as of 7th October 2008 is shown in figure 2. The histogram indicates that the most probable scenario foreseen, was winning the maximized profit by all three simulation methods – the future value varies

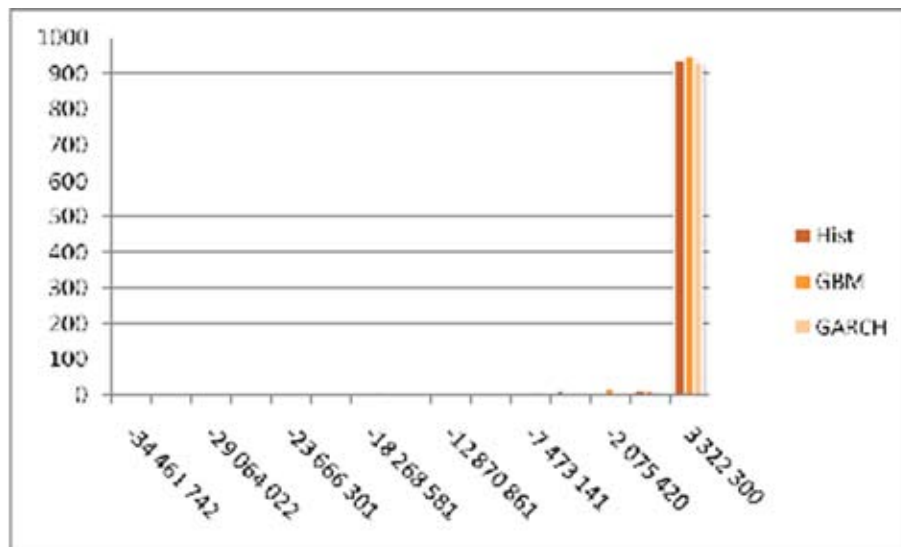
because of the difference in the compounding period. The future value of the realized profit is about 3.3 million forint in more than 90% of the cases according to each simulation.

The mean of the realizations is also high, on average about 2 million forint is the expected profit, which explains the popularity of the structure. The GBM simulation produced the most optimistic forecasts, as the input parameters were taken from a stable period, and the stochastic part was modelled assuming a normal distribution, where the probability of the extreme events is relatively low. The historical simulation proved to be more prudent, allowing tail events with higher probability, but even that method was not able to predict the structural change in the exchange rate movement. During the lifetime of the analysed deal not only the drift rate (average of the daily logreturns) changed significantly: from -0.96% to +10.37% on an annual basis, but the annual volatility increased from 7.83% to 18.88%, compared to the reference period. The GARCH model is most appropriate tool for risk management purposes, as it allows for modelling the empirical observation that a jump in volatility affects the fluctuations of the following period.

There were several measures characterizing the downside, calculated in a way that helped analyse the product from a risk management perspective (table 4). Although the probability of a negative outcome is 4.9%-6.5%, the skewness of the distribution is negative, showing the larger extent of the negative deviations. The maximal loss exceeds even in the GBM model eight times the maximum profit. Moreover, the most prudent GARCH analysis forecasted 26 times higher loss than the capped profit with a probability of 0.1%. The risk measure Value-at-Risk (VaR) that quantifies the maximum loss at a given significance level is widespread in risk management (Jorion 2007). VaR figures were calculated by taking the appropriate quantile of the realizations. According to the GBM model, in 95% of the cases the product results in some profit, the 95% VaR is positive, but the 99% VaR warns for the 1% chance for a higher than 11.9 million forint loss. The VaR figures of the historical simulation are more alarming, and the GARCH model predicts even higher potential losses.

Table 3 - Parameters of GARCH(1,1) model for EUR/HUF logarithmic returns

Expected value equation				
	Coefficient	St. Error	Z-Statistic	Prob.
c	-6.45262E-05	0.0000117511	-0.5491	0.58293
Variance equation				
	Coefficient	St. Error	Z-Statistic	Prob.
a ₀	7.11509E-07	2.79837E-07	2.5426	0.011
a ₁	0.125107	0.0294598	4.2467	0.00002
b ₁	0.8555	0.0337618	25.3392	<0.00001

Figure 2 - Histogram of the profit distribution of profitmax as of 7th October 2008 in HUF

VaR expresses the maximal loss with a probability of α , but the major shortcoming of the measure is that it provides no information about the extent of the loss in the worst outcomes – in $(1-\alpha)\%$ of the cases. An alternative measure answering this problem is expected shortfall (ES) (Acerbi and Tasche 2002), calculating the expected value of the worst $(1-\alpha)\%$ of the cases. The 95% ES shows the average loss to be suffered in the worst 5% of the cases.

The above analysis values the profitmax agreement by itself, without any underlying position. Entering such a deal for speculation meant undertaking the risk of enduring possibly immense losses. All three simulation methods highlighted the possibility for a downside potential corresponding to the actual loss of 19.6 million forint, but with different probabilities. The extent of the loss in fact was weighted with roughly 1% in the historical simulation and the GBM model, and 5% in the GARCH(1,1) model. It is hard to judge according to one realization (the fact figures) whether the ex-ante risk probabilities were under- or overestimated, and the 1-year period from October 2008 has been the most volatile one of the last 20 years in deed. Nevertheless, the risk indications of the GARCH model fit reality best, the other two methods appear to underestimate the risks.

Results of the cash-flow analysis

In order to analyse the product as a hedging tool, it is to be compared to alternative hedging strategies. Assuming that the euro amount – 100,000 EUR at the end of each month of the next year - is to be converted, the future cash-flow has to be analysed. Corporate risk management, being the protection against the cash-flow fluctuation is essential for the companies, uses the measure Cash-Flow-at-Risk (CFaR). CFaR similar to VaR, shows the minimum cash-flow with a certain probability (significance level) of a given period. Usage of profitmax for hedging is set against two other strategies: no-hedge – conversion always at actual spot rates – and average forward hedge – conversion of the euro amount at 256.50 EUR/HUF at each expiry. Figure 3 depicts the distribution of the future value of the cumulated cash-flow, deriving from the 12 conversions, calculated for the 9th October 2009.

In case of forward hedge the future exchange rate is fixed, the variance is perfectly eliminated. The distribution of profitmax is similar to the no-hedge strategy, since in most of the cases, profitmax is knocked-out in 2-3 month, leaving the further expiries unhedged. However the upside potential without hedging is unlimited in contrast to the profitmax.

Table 5 includes the detailed analysis of the cash-flow distribution of the different hedging strategies. The forward hedge offers the highest expected cash-flow ex-ante, and as a consequence of the characteristic of the strategy, the downside risk is eliminated perfectly. The historical simulation describes the cash-flow distribution of profitmax on the most optimistic way, the mean and the downside risk measures are the highest. Interestingly the GBM simulation results somewhat less attractive figures, unlike in the VaR analysis. This change can be explained by the fact, that unfavourable market movements from the structure's point of view are advantageous for the underlying position. Both simulation methods forecasted better downside measures than the no-hedge strategy. Accordingly hedging through profitmax was shown an albeit imperfect, but better hedging strategy than leaving open foreign exchange positions unhedged. GARCH model presents the most conservative risk measures. The analysis demonstrates, that profitmax used for hedge simultaneously restricts the upside potential and generates the lowest cash-flow outcomes.

For exporters, forward hedge is the most favourable hedging strategy ex-ante.

Based on the real market data, the future value of the cash-flow resulted from profitmax, exceeded 332.58 million forint, an amount more than 10 million higher than the cash-flow ensured by the forward hedge (table 6). Because of the weakening of the Hungarian forint, selling euro at the profitmax rate was unprofitable, so the profitmax agreement had not been knocked out, consequently all conversions were executed at 265.00 EUR/HUF, while the average forward rate amounted only 256.50 EUR/HUF. Although the structure by itself generated an almost 20 million forint loss, the higher fx-rates were favourable for the underlying (long euro) position of the exporters.

Table 4 - Results of the profit simulations as of 7th of October 2009

HUF	Hist. Sim	GBM	GARCH
Expected value	2,510,868	2,764,648	1,871,767
VaR 95%	-1,363,010	231,772	-6,328,607
VaR 99%	-17,700,018	-11,940,150	-27,769,151
ES 95%	-10,832,897	-6,811,882	-22,499,448
ES 99%	-22,445,930	-16,922,680	-42,919,145
Minimum	-36,277,997	-25,755,947	-85,778,087
Probability of loss	5.8%	4.9%	6.5%
St. Deviation	3,500,215	2,577,204	6,460,849
Skewness	-5.7621	-6.3944	-6.4665

Figure 3 - Histogram of the cash-flow distribution of profitmax and the alternative hedging strategies in HUF

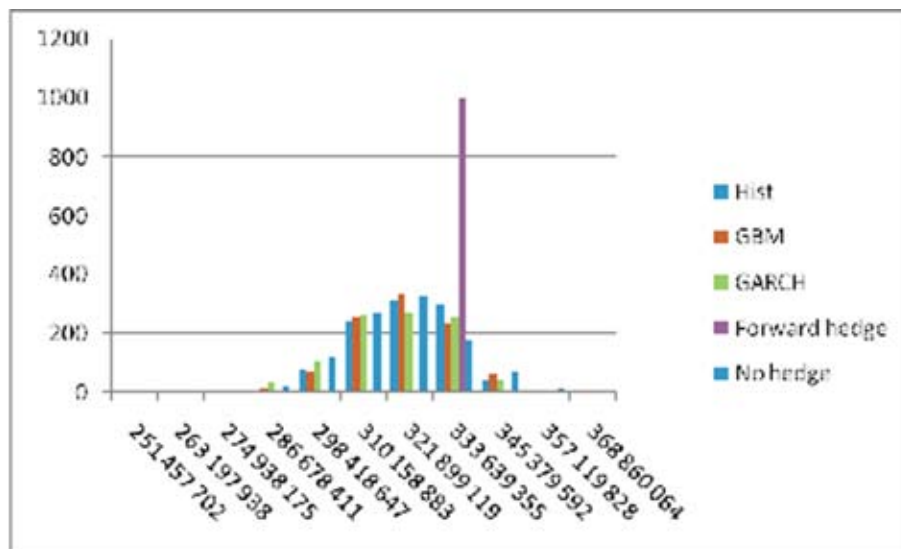


Table 5 - Distribution of the cumulated cash-flow as of 7th of October 2009

HUF	Profitmax				
	Hist. Sim	GBM	GARCH	Forward hedge	No hedge
Expected value	316,085,673	315,413,936	313,406,414	321,914,340	313,574,806
CFaR 95%	295,002,875	293,507,818	288,210,336	321,914,340	291,708,497
CFaR 99%	286,953,227	284,496,433	274,426,854	321,914,340	283,644,164
ES 95%	289,682,505	287,300,025	278,622,455	321,914,340	286,376,860
ES 99%	282,194,209	278,145,562	264,971,002	321,914,340	278,878,923
Minimum	274,451,011	272,452,932	251,457,702	321,914,340	271,132,485
St. Deviation	12,769,443	13,244,331	15,278,502	0	14,177,790
Skewness	-0.1767	-0.0224	-0.3122	0.0000	0.2482

Table 6 - Realized cumulated cash-flow as of the 7th of October 2009

HUF	Profitmax	Forward hedge	No hedge
Realized cash-flow	332,582,067	321,914,340	352,227,558

It is obvious from the above calculations, that for customers with underlying position, profitmax hedge caused an essential opportunity loss, but generated a better than expected cash-flow, so from this perspective the scandal about the product seems to be irrational. The reason of the problems could have been from one hand the fact, that most of the clients entered the deal without any underlying position or many hedgers lost their export income as a consequence of the crisis. On the other hand funding of the enormous mark-to-market loss of the hedge positions could have led to financial difficulties even for hedgers. Despite of the low probability of the loss, quantifying the potential downside ex-ante, could have prevented most of the clients to conclude such kind of deals.

Conclusion

In this paper a special foreign exchange derivative - the profitmax forward agreement - that caused huge losses for several Hungarian companies during the financial crisis, was analysed by using three simulation methods. The large potential loss of the product appeared in all models, but historical simulation and GBM model weighted this scenario with very low probability. GARCH model proved to be the most adequate tool for risk analysis, as it described the downside the most realistically.

It was shown, that the profitmax agreement is not an appropriate device for hedging purposes, being it is not able to grant a worst-case exchange-rate for the whole exposure. In case of falling rates, the protection ceases to exist after the first 2-3 expiries. However clients with underlying position benefited from using it for hedging, instead of the plain vanilla forward hedge. Financial distresses were caused for speculators, and speculation was definitely encouraged by the financial institutions. Whether the banks were unable to judge the risk appetite of their clients correctly, or their incentives prevented them from a more explicit risk-warning or the taken risk was not foreseen even for the sales force of the banks, remain open questions.

This situation of asymmetric information is to be solved by the financial authorities. The optimal solution however is not prohibiting banks from financial structuring, but requiring more complex risk analysis to make the downside much more transparent for the clients.

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