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## Contents

# ECONOMISTS' FORUM

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# Banking Sectors in South-Eastern European Economies

YIWEI FANG[1] – IFTEKHAR HASSAN[2] – KATHERIN MARTON[3]

**Abstract**

It has been a major achievement that within a decade subsequent to military conflicts, embargo, and crises in the Western Balkan region, a privately owned banking sector developed in SEE that provides financial services similar to those of Western Europe. Rapid privatization ended government interference in the banks and foreign ownership contributed to the build-up of trust of the population that was fractured in several countries through actions of the central bank and other authorities.

The global economic crisis exposed some of the strength and vulnerabilities of SEE countries where mostly during the last decade banking sectors moved from state- and collective ownership to predominantly foreign ownership. Since this is a relatively new phenomenon, government policy makers need to adopt regulations that increase the benefits that foreign banks contribute to the local economy but also reduce some of the adverse impacts that are associated with foreign bank ownership.

**Keywords**: South-Eastern Europe, banking sector, financial intermediation, foreign banks

**JEL Classification**: G20, 21

Two decades after the political changes of 1989, the South-Eastern European (SEE) region went through dramatic political and economic transformation. In the formerly centrally planned economies of Bulgaria, Romania and Albania as well as in the successor states of the former Yugoslavia, the transition to market economies is largely completed. Compared to countries of Central and Eastern Europe (CEE), the transition in SEE was accompanied by far more political turmoil and instability. This slowed down the reform process and delayed major economic restructuring during the first decade. With the political stabilization following the

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end of the Kosovo war and democratic changes in the Federal Republic of Yugoslavia in 2000[4], the region experienced sustained economic growth and the pace of economic reforms accelerated. Bulgaria and Romania joined the European Union (EU) in 2007 and are to be followed in the near future by Croatia. Despite such progress, countries of the Western Balkan remain Europe's economically least developed region. Reducing the economic gap with the EU will require concerted and sustained efforts over an extended period. Development of the financial sector will play an important role in this process. In most transition economies capital markets are still in early stages of development, and it is the commercial banking sector that assumes key function in financial intermediation. It is within this framework that this paper aims to assess the state of commercial banking sectors in SEE countries. Though their restructuring in the region began later than in CEE, once the process of privatization of state-owned banks started the transition to a privately owned banking sector took place within a relatively short time. Their stability withstood the test of the recent global financial crisis. This is an opportune time to analyze the major characteristics of the banking sectors that evolved and identify features that may shape future development.

The transition process of banking sectors in CEE countries is covered extensively. Due to its relatively late start, and smaller size, the SEE has region received less research attention. Though the transition experience of the two regions was similar in many aspects, different historical legacies, subsequent political events and timing of reforms also contributed to differences in the two regions. Since the large economic heterogeneity of SEE is an important hallmark of this region, this inevitably affected financial sector development of the countries. Our analysis of the region shows that despite such variations, the banking sectors that evolved in the countries are quite similar in terms of ownership structure and other key financial sector development indicators. We also find that though the arduous process of restructuring resulted in privately owned and rather efficient banking sectors in SEE countries, financial sector development remained at relatively low levels.

The paper is organized as follows: Section 1 presents the process of

[4] In 2000. this included Serbia and Montenegro

transition in SEE countries, including Bulgaria, Romania and countries of the Western Balkan region[5]; Section 2 analyzes the global trend of banking sector internationalization, the broader context for SEE; Section 3 reviews salient literature on the performance of foreign-owned banks in local economies; Section 4 assesses financial sector development in SEE countries by using generally accepted indicators and compares them to other middle income countries as benchmark; Section 5 concludes the paper.

**1. The transition process of banking sectors**

In Bulgaria, Romania and Albania, the financial sector during socialism followed the Soviet-model of mono-banking system where the state-owned bank performed central banking functions and held accounts of state-owned enterprises. There were also specialized banks such as the national savings bank and foreign trade bank. The function of the system was not financial intermediation in the sense of market economies. Financial needs of enterprises were met largely through the budget and banks had more of an accounting function. The overlaying role of centralized political decision-making characterized allocation of credit throughout the socialist system (Winiecki, 1991). The former Yugoslavia abandoned the mono-banking model in the late 1950s and established a decentralized system of banks under worker management. In 1985, for example, 170 banks operated in the country and it had the most advanced banking sector in the region (Radzic et al. 2008). The former Yugoslavia held also extensive trade relationships with Western Europe. In 1989, it was well placed to move towards a market economy. There were, however, large internal economic differences among regions. Slovenia and Croatia in the north were far more advanced than the Western Balkan region.

In Bulgaria, Romania and Albania, unstable and weak macroeconomic conditions during the first decade of transition delayed privatization of banks. During the early 1990s, however, governments promoted the entry of domestic banks through very liberal policies, such as low mini-

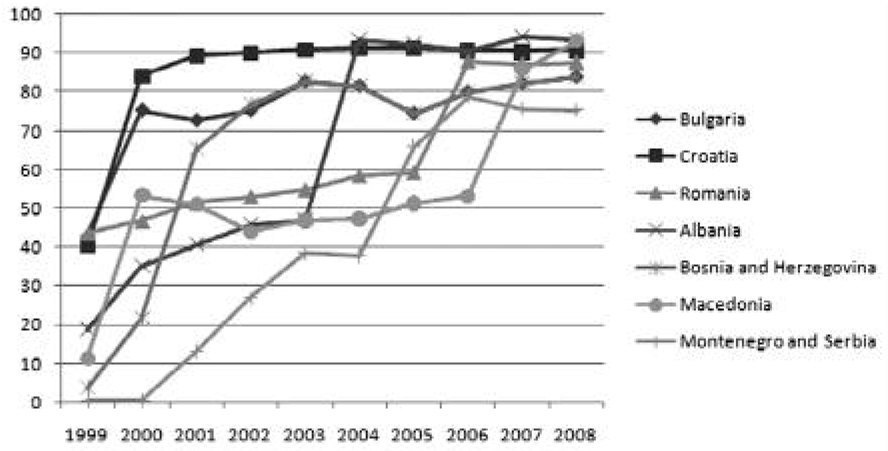
[5] Though Slovenia was part of former Yugoslavia and geographically is part of South-Eastern Europe, in 2007 it joined the Organization of Economic Co-operation and Development and has a developed country status. Due to this difference from other parts of the region we did not include Slovenia in our analysis. Due to limitations of data we also omit coverage of Montenegro and Kosovo.

mum capital requirements. Regulations for entry of foreign banks were restrictive. Under weak bank regulatory systems and government intervention in bank management state-owned banks continued to lend to ailing state-owned enterprises which led to the accumulation of large non-performing loans. In 1996, for example, about 60 % of Bulgarian assets were non-performing and the estimated non-performing loans of the three major Albanian state-owned banks amounted to 90% of the assets (Backe et al. 2006). These problems led to banking sector crises in 1996-97 in Bulgaria, and in the late 1990s in Romania and Albania. Clean-up of the banking sectors by the respective governments was costly and time-consuming. It also underlined the importance of a rapid privatization through foreign investors. In the late 1990s, all three countries started major privatization programs, with the pace in Bulgaria more rapid than in Romania and Albania.. By the early 2000s the banking sector privatization was largely completed.

In 1989, the socially-owned banks in the former Yugoslavia were transformed to joint stock companies, and in 1991 their privatization began. Banks had to submit a privatization plan to the government. If the government did not approve it, the bank became state-owned. During this process, the ownership of many banks reverted to the state. Consequently, following the break-up of Yugoslavia, and the independence of Croatia, Macedonia and Bosnia and Herzegovina in 1991, a relatively large number of banks operated in these countries. Many of them, including newly formed private domestic banks, were undercapitalized and managed inefficiently. At the end of the 1990s, all three countries experienced banking crisis and many of the small banks went bankrupt. Subsequent to the crises the privatization process accelerated.

As a result of over a decade of military conflict, political and economic isolation, and hyperinflation, restructuring of the financial sector started later in Serbia than in other SEE countries. During the Balkan wars the central bank confiscated the foreign exchange reserves of the banks, which affected adversely the trust of the population towards financial institutions. In 2000, the newly elected government improved the banking regulatory system and began privatization of state-owned banks. By 2009, about 70 % of the sector's assets were privatized through foreign banks.

The brief review above shows that despite differences in initial conditions and subsequent political events in countries, the process of restructuring of the banking sector and its outcome were similar. Liberal entry policies for new banks, inadequate bank regulatory and supervisory legislation, delays in the privatization of state-owned banks amidst deteriorating conditions of the real sector of the economy contributed to banking crisis in Bulgaria in 1996-97, in Albania in 1997, Croatia in 1998-99, Romania in 1999-2000, Bosnia and Herzegovina in 2001, and




*Source: based on EBRD, Transition Report, London, various issues*

**Chart 1. Foreign ownership in the banking sector, percentage of assets**

in Serbia until 2004. The high costs of bailouts for governments underlined the urgency of rapid privatization and the need to recapitalize the sector through foreign investors. International lending institutions that provided financial assistance and advice to countries during the banking crises also supported rapid privatization through foreign banks. Implementation of these programs also coincided with the initiation of negotiation for accession to the EU by Bulgaria, Romania and later Croatia. Under the terms of the accession agreement governments committed themselves to major revision of their banking regulation and to full opening of the sector to investors from the EU. These agreements, together with the political and economic stabilization of the region, improved the investment climate of the region for foreign banks. As can be seen in Chart 1, and Appendix 1, with the completion of the privatization of banking sectors in SEE countries became largely foreign owned.

**2.1. Internationalization of banks**

Large-scale entry by foreign banks to SEE followed the trend of the past two decades marked by the global expansion of banks. Traditionally, two major theories addressed internationalization of banks. On the macro level, foreign direct investment (FDI) in the banking sector was linked to bilateral trade flows between two countries (Grosse and Goldberg 1991, Williams, 1998; Yamori, 1998). On the micro-level, expansion of banks was explained by the motivations of banks to follow their customers to foreign markets that they can provide them financial services (Caves, 1971; Dunning, 1993; Rodriguez-Clare, 1996). Foreign expansion of U.S. banks during the 1970-1980 period found empirical support for this theory (Markusen and Venables, 1997).

During the past two decades, with increase of FDI flows in the global economy, the traditional pattern of such flows changed in the banking sector. Clarke et al. (2003), for example, argue that while the "follow the customer motivation" may explain expansion of banks to developed markets, presently, it is less relevant to developing countries. Entry of banks to high-growth emerging markets is primarily motivated by local profit opportunities and the competitive advantage that they enjoy vis-à-vis domestic banks (Focarelli et al. 2000). Since the 1980s, in Latin American and East Asian countries, increase in foreign ownership of banking sectors was also associated with financial crises. During such episodes, governments lifted former restrictions on foreign ownership in the financial sector and allowed foreign banks to acquire ill-performing domestic banks. International lending organizations that gave financial support and advice to countries in crises also advised governments to liberalize the financial sector and reduce or eliminate restrictions on foreign ownership. Most of the recent growth in foreign expansion of the banks took place in developing countries. Though there have been a number of large mergers and acquisitions in developed countries, overall the share of foreign-owned banks remained relatively low. Table 1 shows that the during the last 1995-2005 period the largest increase in foreign bank ownership took place in Latin American and Caribbean countries and to a lesser extent in Asian countries.

**Table 1. Foreign share of total banking assets, %, 1995 and 2005**

| Region | 1995 | 2005 |
|---|---|---|
| East Asia | 7 | 3 |
| Latin America and the Caribbean | 11 | 37 |
| Middle East and North Africa | 7 | 15 |
| South Asia | 0 | 6 |
| Sub-Saharan Africa | 20 | 9 |

*Source: Claessens et al. 2008.*

The exceptionally high share of foreign ownership that characteries CEE and SEE regions is unprecedented in contemporary times[6]. Only a few, mostly tax haven island economies such as Barbados and Madagascar have banking sectors with similarly high foreign ownership.

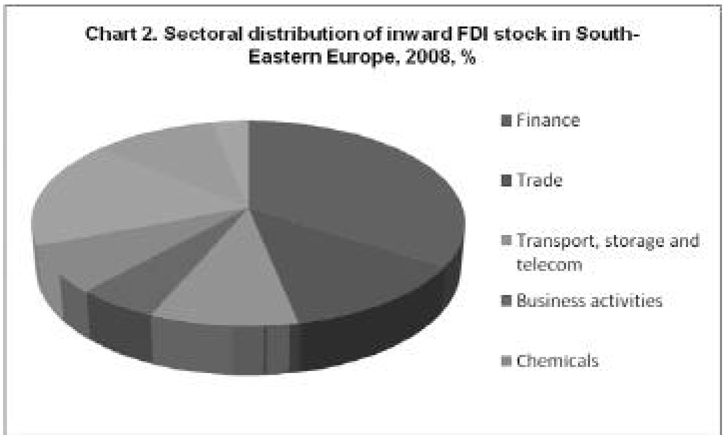
### 2.2. Foreign banks in SEE

A few banks from the EU dominate banking sectors in SEE. Most of these are based in the neighboring countries, with the largest presence of Austrian, Italian, and to a lesser extent, French, Greek and Turkish banks. Appendix 2 shows the branch network of these banks in SEE countries. It is interesting to note the all the countries are dominated by a relatively few foreign banks. These banks also held large market shares in most CEE countries, markets that they entered during the privatization process of the 1990s. With changing regulations in the Commonwealth of Independent States, these same banks are currently expanding to countries of that region. With few exceptions, the largest European banks have limited presence in SEE. Most of the banks that operate in the region are medium-sized and liberalization of Eastern Europe presented them opportunities for growth. Since many of the state-owned banks were privatized subsequent to major banking crises, foreign banks acquired assets at favorable prices and also ensured guarantees from the government related to potential non-performing loans that originated prior to privatization. Foreign

[6] High foreign ownership of the banking sector was prevalent, for example, in several Central and South Eastern European countries around the turn of the 20th century.

banks also entered SEE countries through de novo formation. This form was used mostly by Greek and Turkish banks, while Austrian and Italian banks established their operations mostly through the privatization process (UNCTAD, 2010).

A distinct feature of FDI inflows to SEE, and particularly to the Western Balkan region, is the dominance of such flows by the financial sector. As can be seen in Chart 2, FDI in the financial sector accounted for 32 % of total inflows, the largest share among sectors. With the exception of Croatia and Romania, a hallmark of FDI inflows to the SEE region is its high concentration to a few services sector, primarily finance, real estate, and telecommunications and it's their relatively low share in the manufacturing sector. This contrasts with the sectoral distribution to most CEE countries, where FDI inflows are more evenly distributed among the services and manufacturing sectors. In these countries FDI played an important role in establishing export-oriented manufacturing. This phenomenon, with the exception of Croatia, is largely absent in SEE countries. Foreign banks' motivation to enter SEE was not to "follow the customer" rather, it was the local market opportunity and their strong competitive advantage vis-à-vis domestically-owned banks. The concentration of




*Source: UNCTAD, World Investment Report, 2010*

**Chart 2. Sectoral distribution of inward FDI stock in South-Eastern Europe, 2008, %**

banks to a few neighboring source countries is consistent with gravity models assuming that geographical distance of two countries is major determinant of FDI flows (Guimaraes et al. 2000).

### 3.1. Performance of foreign-owned banks in the host country

Internationalization of the banking sector and its implications for the host economies were researched extensively. Within this context, it was investigated whether foreign-owned banks behave differently than their domestically-owned counterparts. Generally, the positive contribution of foreign-owned banks to the host economy received support in the literature. Foreign-owned banks were found to mobilize low cost funds and improve allocation of resources (Goldberg and Saunders, 1981; Gelb and Sagari, 1990, Terrell, 1986; Bhattacharaya, 1993). In several country case studies, mostly undertaken in developing countries, foreign owned banks were found to be more cost efficient than domestically-owned ones. This was largely attributed to the ability of the local subsidiaries to access lower costs funds and technology of the parent company. Study of banks in 80 countries during the 1988-1995 periods by Claessens et al. (2001), however, resulted in more differentiated findings. Their research found that in developed countries foreign owned banks operated with lower interest margins and profits than domestic banks but in developing countries, the opposite was true. Their findings draw attention to the importance of local economic conditions on the performance of foreign banks.

Several studies investigated the relationship between performance and ownership of banks in transition economies. Country case studies, for example, for Croatia (Jemric and at al., 2002), Poland (Nikiel et al., 2002), and Hungary (Hasan et al., 2002) and for a sample of 20 transition economies (Fries et al., 2005), found that foreign owned banks were more efficient than domestic private- or state-owned banks. These studies covered the 1990s, the first decade of the transition when problems of the real sector impacted state-owned banks adversely and the initial weak regulatory systems allowed entry of undercapitalized small private banks. A number of recent studies that investigated the second decade of transition found a different landscape. Subsequent to the banking crises that all countries experienced, weak domestically owned banks exited the market. Those that survived the instabilities of the first decade of transition, over time, gained experience, and improved their technological and managerial know-how. In the 2000-2007 periods domestically-owned banks, on average, operated with similar cost efficiencies than foreign- owned banks. Two important comprehensive studies analyzed banking sectors in the post 2000 period. Firstly, Zajc et al. (2009) studied performance of banking sectors during the 1996-2006 periods in 8 ECE countries that in 2004 joined the EU. Cost-efficiency of banks during the ten-years was not related to their ownership; rather, market concentrations explained differences among countries. Similarly, the recent study of Yiwei et al. (2010) of banking sectors in 6 South-East European countries during the 1998-2008 periods found no significant cost efficiency differences between foreign- and domestically owned banks. Their findings were, however, consistent with earlier literature, that foreign owned banks were significantly more profit efficient than domestically owned banks.[7] They attributed the higher profitability of foreign owned banks to their competitive advantage in offering a wider range of products than domestic companies and their ability to extract higher rents on those products.

As can be seen in Table 2, the rates of return on investment in SEE countries are significantly higher than in Western European countries, home countries of the banks. Though rates of returns had declined from the much higher levels of the late 1990s, they remained well above that of other European countries.

### 3.2. Lending practices

Research on the role of ownership on lending practices addressed two major issues. Firstly, do foreign- and domestically-owned banks have different customer base? Secondly, does ownership influence lending behavior during periods of financial crisis? Research on the allocation of credit by banks in Latin American and Asian developing countries found some evidence that foreign banks cater primarily to large firms, and those located in urban areas (Berger et al. 2001). Small companies which are often “informationally opaque”, and require ‘relationship banking’ and firms in rural areas were found to be served mostly by domestically owned banks

[7] Profit efficiency refers to a bank’s ability to earn higher profit with the same bundle of inputs.

**Table 2. Bank return on assets, percentage, in SEE and selected EU countries**

| **Country/Year** | **2005** | **2006** | **2007** | **2008** |
|---|---|---|---|---|
| Albania | 1.4 | 1.4 | 1.6 | 0.9 |
| Bosnia&Her. | 0.7 | 0.9 | 0.9 | 0.4 |
| Bulgaria | 2.1 | 2.1 | 2.4 | 2.1 |
| Croatia | 1.6 | 1.5 | 1.6 | 1.6 |
| Macedonia | 1.2 | 1.8 | 1.8 | 1.4 |
| Romania | 1.9 | 1.7 | 1.3 | 1.6 |
| Serbia | 1.1 | 1.7 | 1.7 | 2.1 |
| **EU** | | | | |
| Austria | 0.6 | 0.7 | 0.8 | 0.1 |
| France | 0.6 | 0.6 | 0.4 | 0 |
| Germany | 0.4 | 0.4 | 0.3 | -0.3 |
| Italy | 0.7 | 0.8 | 0.8 | 0.3 |
| Portugal | 0.8 | 0.9 | 1.1 | 1 |

*Source: International Monetary Fund, Global Financial Stability Report, 2010*

(Mian, 2006). Foreign-owned banks in Poland in the mid-1990s were found to prefer to lend to large commercial firms while domestically-owned banks catered mostly to smaller companies (Nickiel, et al.2002). A study undertaken in 2005 on the lending practices of 220 banks in 20 transition economies concluded that foreign-owned banks lent a higher proportion of their assets to consumer mortgage loans and foreign subsidiaries than did domestically–owned banks (DeHaas et al. 2007). The study also identified a significant relationship between bank size and customer base; smaller banks were found to provide financial services mostly to small- and medium-sized companies and large banks to large companies.

Access to credit by various types of enterprises was studied in a comprehensive study of over 8000 firms in 20 transition economies by Brown et al (2010).[8] Their research found that in Eastern European transi-

[8] Among the countries the following SEE countries were included: Albania, Bulgaria, Bosnia, Croatia, Macedonia, Romania and Serbia

tion economies the high interest rates of loans, the collateral requirement and the cumbersome conditions of loan application discouraged a very high percentage of small firms to apply for loans. The proportion of discouraged small firms increased with the higher share of foreign ownership in the sector.

With the growing participation of foreign owned banks in several developing countries the issue of the relationship between bank ownership and lending practices during episodes of financial crisis gained importance. Such research was motivated by the concern that foreign- owned banks may cut back their lending in the local market during financial crisis and thus, affect financial stability adversely. Research on lending behavior during the financial crises of the 1980s and 1990s in Latin American and East Asian countries resulted in inconsistent findings. Peek and Rosengreen (2000), for example, found that during the financial crisis in Argentina in the early 2000s, foreign banks did not curtail their local lending. In Malaysia, on the other hand, during the Asian crisis, a sharp drop in foreign bank lending took place (Detragiache and Gupta, 2004). Comparing pre- and post crisis lending by foreign banks in 10 CEE countries that experienced financial crises during the 1990s, De Haas et al. (2006) found no significant curtailing of loans during the crisis period. They concluded that foreign banks, by maintaining lending levels, contributed to the stabilization of the economy. Lending by foreign banks was, however, subject to economic conditions in their home country. For this reason, De Haas et al. (2006) suggested governments in transition economies that they diversify the sources of country origin of foreign banks.

Due to the high concentration of foreign banks in SEE from a few EU countries, vulnerabilities of these countries became a major concern during the recent global financial crisis. Sudden stops in credit flows to the local economy could have greatly aggravated the crisis. Risks for the banks was also high since for some of them loans to the region accounted for a major share of their assets and profits. The gravity of this problem, both for parent companies and their local subsidiaries in SEE (and CEE) and their respective economies, required a concerted effort by all major constituents involved. This action, referred to as the Vienna Initiative, brought together representatives of home and host governments of the banks, bank regulators, and representatives of major parent banks with extensive subsidiary network in the CEE-SEE region.

### 3.3. The Vienna Initiative

By the late 2008, the global financial crisis hit CEE, and somewhat later SEE, strongly. During the credit boom of 2004-2007, there were large cross border inflows to SEE through the banks. Several countries had major current account deficits and relied on outside financial flows not only for credit but also for support of their foreign exchange system. A sudden stop of credit flows from parent banks could have had serious regional implications. Losses from the region also created major vulnerabilities for Austrian, Italian, Greek and Turkish banks that were exposed heavily to the region. Since the mandate of the European Bank for Reconstruction and Development (EBRD) has been to ensure successful transition of former socialist countries to market economies, it assumed a leading role in co-ordination of rescue effort. The concerted international intervention involved provision of financing by the International Monetary Fund (IMF) to governments where current account deficits and foreign exchange system support required access to foreign loans. In 2009, IMF granted loans to Romania, Serbia, Bosnia and Herzegovina, and Kosovo. The conditions of IMF loans, and of other European Union support programs, included commitment by parent banks to maintain their existing exposure in SEE and CEE countries and recapitalization of their subsidiaries. Such commitments sought to avoid potential home bias on the part of major banks and their withdrawal of funding from subsidiaries in SEE (and CEE countries). Though the initial agreement involved only commitments in countries that received IMF support, subsequently it was extended to the entire SEE region (EBRD, 2010). As part of the agreement, governments in SEE (as well as in CEE) committed themselves to provide local currency liquidity to banks, irrespective of their ownership. This concerted effort was successful in preventing large outflows of funds from the region. During the last quarter of 2008 and the first quarter of 2009, BIS reporting banks in transition economies reduced their assets by 4 percent (EBRD, 2010).

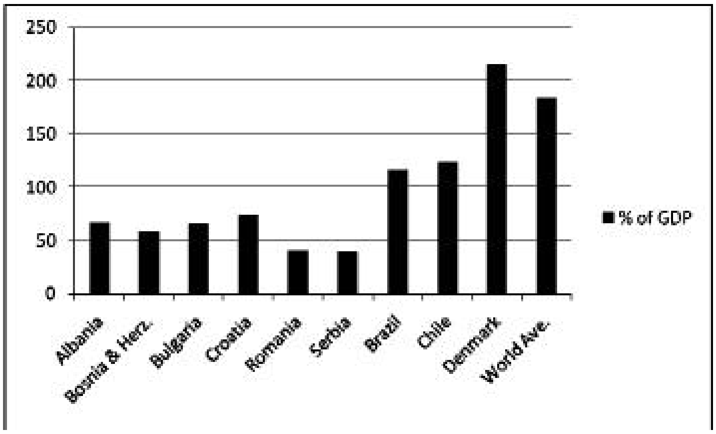
## 4. Financial sector development in SEE

The role of financial sector in economic development is well-documented (Greenwood and Jovanovic, 1990; King and Levine, 1993; Levine, 1996). There is substantial research evidence that even after controlling for per capita GDP, countries with well-developed financial sector experience higher growth rates. Private sector credit, (measured as percentage share of GDP), was found to be a good predictor of subsequent economic growth (Levine et al. 1999). Relatively easy availability of credit was also found to encourage development of capital-intensive industries (Rajan et al. 2004). Ease of access to credit by the small- and medium-sized companies was also related positively to income distribution and poverty rates (Beck et al. 2004).

The commonly used indicator of financial sector development is the share of domestic credit to the private sector in relation to GDP (Levine et al., 1999; Berglof and Bolton, 2002). In transition economies, both in SEE and CEE, prior to privatization of state-owned banks credit expanded rapidly, mostly to finance the loss making state-owned enterprises. The financial crisis that ensued in all countries ended the credit expansion. With the privatization of banks, the new foreign owners assumed initially very risk averse posture. In 1999, with the exception of Croatia, domestic credit to the private sector was very low, ranging from 3 % in Bosnia and Herzegovina to 12 % in Bulgaria EBRD, 2000). Many banks held most of their assets in government bonds or other securities. In Albania, for example, in 2004, 70 percent of the banks assets were invested in treasuries (EBRD, 2006)

With high global liquidity in the 2003-07 period countries in SEE experienced very high growth rates of credit expansion, although from a very low base. In 2008, the range of private sector credit among countries was quite large, ranging from 39 % of GDP in Serbia to 75 % in Croatia. Following Serbia, the share of private credit to GDP, with 40.9 %, was the second lowest in Romania. In 2008, with the global financial crisis, the credit expansion came to a sudden halt.

Though countries of SEE experienced a credit boom in the 2003-07 periods, in 2008 with an average share of the private sector credit to the GDP of 57 %, financial sector depth is comparatively underdeveloped. Private sector credit to GDP ratios in other middle income countries are around 100 percent and the ratios are above 200 percent in developed countries. In 2008, the world average of private sector credit ratio to GDP was 185 % (World Bank, 2010).




*Source: World Bank, Indicators database*

**Chart 3. Domestic credit to the private sector 2008**

Banking sector assets in countries of SEE are very small, both in absolute terms and as percentage share of GDP. As can be seen in Table 3 with 85 billion euros, total banking sector assets are highest in Romania, to be followed by 49 billion euros in Croatia. In 2008, total banking sector assets in 5 SEE countries, for which data was available, amounted to 203 billion euros, about 6 % of the 31,363 billion euros for the Euro region (Bank Austria, 2009). In terms of percentage share of GDP, banking sector assets for the euro area were 346 %, while in SEE countries only in Croatia and Bulgaria exceeded 100 %. With a ratio of 67 percent to GDP, the lowest share of banking assets to GDP was in Romania.

**Table 3. Banking Sector Assets, 2008**

| Country | Total Bank Asset | |
|---|---|---|
| | in bil. Euro | % of GDP |
| Bulgaria | 37 | 108 |
| Bos.&H. | 11 | 86 |
| Croatia | 49 | 106 |
| Romania | 85 | 67 |
| Serbia | 21 | 70 |
| Euro Area | 31,631 | 346 |

*Source: Bank Austria, 2009*

**5. Conclusions**

It has been a major achievement that within a decade subsequent to military conflicts, embargo, and crises in the Western Balkan region, a privately owned banking sector developed in SEE that provides financial services similar to those of Western Europe. Rapid privatization ended government interference in the banks and foreign ownership contributed to the build-up of trust of the population that was fractured in several countries through actions of the central bank and other authorities.

The salient feature of banking sectors in SEE countries is the very high share of foreign ownership and the very limited role that domestic private and state-owned banks play. As discussed in the paper, this development was driven by serious banking crises that required rapid privatization. The urgency left few alternatives for governments than foreign buyers. (An exception from this path was followed in Slovenia). Since in present times such high foreign ownership of the banking sector is a new phenomenon, its long- term benefits and costs to the countries are hard to assess. The literature, discussed above, gives a differentiated picture, higher efficiencies of foreign banks tend to show trade-offs with higher profits by such banks, and some evidence suggest that foreign banks are less inclined to service smaller companies than do domestic banks. The validity of these findings for SEE countries would need to be monitored over time. Limited access to finance by small- and medium sized companies would impact especially adversely countries of the Western Balkan where most of the firms are relatively small and job creation and growth will depend on access to credit by these firms.

High foreign ownership in an industry is associated generally with high dependency on foreign decision makers and their profit objectives. Operations of foreign banks in SEE reflects the strategic importance of these markets. During the 2003-07 periods, banks increased sharply their lending at interest rates that were far above levels in western European countries. In SEE countries, the costs of financial intermediation were very high. For foreign banks an important source of profits was their ability to obtain funds at low costs from their parent company. Since these funds were in foreign currency, to avoid foreign exchange exposure, banks matched their position by lending in foreign exchange to local consumer. In the 2005-2008 periods, for example, over 60 percent of the loans in SEE were in foreign exchange (EBRD, 2010). This shifted the foreign exchange risk from the banks to unhedged borrowers. When in the wake of the recent global financial crisis foreign exchange rates were devalued in several SEE countries, substantial costs were imposed on local borrowers.

Though the Vienna Initiative was successful in preventing a large scale withdrawal of funds by foreign banks from SEE countries, the credit boom of the 2003-07 periods was followed by a major drop in new lending. These large swings in boom and subsequent drying up of loans were more pronounced in SEE countries than in Latin American and Asian developing countries (Kamil et al. 2010). The large fluctuation in credit availability imposed high adjustments costs on local economies.

The global economic crisis exposed some of the strength and vulnerabilities of SEE countries where mostly during the last decade banking sectors moved from state- and collective ownership to predominantly foreign ownership. Since this is a relatively new phenomenon, government policy makers need to adopt regulations that increase the benefits that foreign banks contribute to the local economy but also reduce some of the adverse impacts that are associated with foreign bank ownership.

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**Appendix 1. Characteristics of banking sectors in South-Eastern Europe, 1999-2008**

| **Country** | **No. of total banks** | | **Market share of the top 5 banks** | | **% Asset share of foreign-owned banks** | | **% Asset share of state-owned banks** | |
|---|---|---|---|---|---|---|---|---|
| | 1999 | 2008 | | 2008 | 1999 | 2008 | 1999 | 2008 |
| Bulgaria | 34 | 29 | | 57 | 42.8 | 83.9 | 50.5 | 1.8 |
| Croatia | 53 | 34 | | 76 | 40.3 | 91.2 | 39.8 | 4.7 |
| Romania | 34 | 31 | | 54 | 43.6 | 87.9 | 50.3 | 5.9 |
| Albania | 13 | 17 | | 15 | 78.2 | 94.2 | 81.1 | 0 |
| Bosnia&Her. | 91 | 32 | | 22 | 76.0 | 95 | 75.9 | 3.2 |
| Macedonia | 23 | 18 | | >80 | 2.5 | 93.1 | 2.5 | 1.4 |
| Montenegro | n.a. | 10 | | >80 | n.a. | 91.9 | na | 0 |
| Serbia | 75 | 37 | | 46 | 0.4 | 78.7 | 8.9 | 14.9 |

*Source: EBRD, Transition Report, various issues.*

**Appendix 2. Total number of branches in SEE countries, 2008**

| **Bank/Country** | BG | RO | Croatia | Albania | Serbia | BH | Total SEE |
|---|---|---|---|---|---|---|---|
| Raiffeisen Int. | 197 | 557 | 79 | 102 | 103 | 100 | 1,185 |
| UniCredit | 269 | 259 | 140 | | 72 | 161 | 901 |
| Société Générale | 142 | 932 | 117 | 40 | 88 | | 1,413 |
| Erste Bank | | 641 | 119 | | 68 | | 828 |
| Intesa Sanpaolo | | 92 | 230 | 33 | 230 | 52 | 637 |
| OTP | 379 | 105 | 105 | | 95 | | 724 |
| KBC | 139 | | | | 65 | | 204 |
| EFG | 223 | 293 | | | 123 | | 639 |
| N. B. of Greece | 280 | 149 | | 29 | 104 | | 628 |
| ING | 2 | 120 | | | | | 122 |
| Volksbank | | 246 | 28 | | 26 | 50 | 350 |

*Source: Bank Austria Market Research, 2009.*

# Framing Rural Employment Policy in the European Union in the Context of Sustainable Regional Development

ANDREW F. FIELDSEND[1]

**Abstract**

Many respected academics have questioned the appropriateness of the continuing close link between the Common Agricultural Policy and its 'rural development' measures. The European Union (EU) Framework 7 research project 'RuralJobs' included case study research on current employment patterns and opportunities for, and constraints on, rural economic diversification in five contrasting NUTS2 regions across the EU. As a contribution to the current debate on the shape of EU rural and regional development strategies for the period 2014-2020, this paper presents the results of this analysis. Rural areas differ in their accessibility to urban centres with a population of 50,000 or more, but smaller population centres can be important employment and service centres for their rural hinterlands. An urban-focused approach to regional development could precipitate a 'race to the bottom' by excessively targeting funding at urban centres and contributing to the economic and social decline of the rural hinterlands. To comply with the priorities of the EU's Europe 2020 strategy, namely smart, sustainable and inclusive growth, regional development strategies should include a distinct rural component which recognises the potential contribution of natural capital, and therefore rural areas, to achieving a competitive regional knowledge economy.

**Keywords**: rural employment, European Union, regional development, accessibility

**JEL classification**: O18, Q01, R12

## Introduction

Many respected academics have questioned the appropriateness of the continuing close link between the Common Agricultural Policy (CAP) and its 'rural development' measures. At European Union (EU) level Shucksmith (2010) relates how the term 'rural development' has acquired

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a new and highly contested meaning through the establishment of the CAP's second pillar, the rural development regulation (RDR). The CAP remains primarily a structural adjustment policy for agriculture and Shucksmith (2010) cites Bryden and Hart who wrote "the profound weakness of the [new] RDR becomes increasingly apparent when the scope of its menu of eligible measures is compared with what needs to be addressed if failing rural areas are to be turned around economically and demographically". Gorton et al. (2009) describe how in the New Member States (NMS) non-farming related interests are poorly represented and have struggled to be effectively included in RDR measures.

Marsden (1998) highlighted the need for a more regionally and spatially orientated rural development policy and Marsden (1999) suggested that "[o]ne possibility is a new Rural Development Objective and Fund, seeking to integrate elements of CAP, Regional and Social Funds, and implemented through Rural Area Programmes at regional/local levels ... They might also involve more refined definitions of priority areas through a new typology of rural areas at EU level, and methods of defining priorities from a cohesion point of view". In the current (2010) context the relevant 'elements' of the CAP would be Axes 1, 3 and 4 of Pillar I. Pillar I and Axis 2 of Pillar II focus on direct payments to farmers rather than rural development in its broader sense. The former has been more effective in maintaining farm employment rather than creating new jobs (EC, 2006) while agri-environmental payments (Axis 2) have led to little direct creation of jobs (Mills et al., 2010).

The results of the EU Framework 7 research project "New Sources of Employment to Promote the Wealth-Generating Capacity of Rural Communities" (acronym: RuralJobs) were expected to facilitate a better targeting of rural development measures and future evolution of rural development policies in line with the Lisbon Strategy. The research was founded on three hypotheses (Fieldsend, 2008):

- That a territorial approach to improving the wealth generating ability of rural areas through the creation of new sources of employment is required, whilst recognising the unique dimension of agriculture and other land-based industries in the rural economy;
- Initiatives to create new sources of employment in rural areas must take account of the existence of markets for the products of labour,

whether these are in the primary, secondary or tertiary sectors. Frequently, the largest markets are in urban areas;

• Rural areas in different parts of the EU are fundamentally different from each other in many respects and that a single, EU-wide 'solution' or 'strategy' for creation of rural employment is not appropriate.

It was anticipated that, through the study of a representative selection of regions, it would be possible to identify general principles which can be applied to different 'types' of rural area. The typology chosen for RuralJobs (Raupelienë, 2009) was applied at NUTS3 level and was based on an EU DG Regio study (Dijkstra and Poelman, 2008) which combines a new classification of remoteness, based on driving time to the closest city (of 50,000 inhabitants or more), with the OECD classification of rurality based on population density (OECD, 1994). RuralJobs combined this with the criterion of GDP per head, as used, for example in the EU Fourth report on economic and social cohesion (EC, 2007), with a threshold of 50% of the EU-27 average. The result is twelve 'types' of NUTS3 region of which four are urban. Of the remaining eight, there are very few intermediate, remote regions regardless of level of GDP, leaving six 'types' of rural area which occur widely.

The OECD classification system for regions (i.e. predominantly rural, intermediate and predominantly urban) provides a systematic, if crude, assessment of their rurality. Within this system many kinds of rural space exist and the future development trajectories of different types of rural area will differ. The choice of 50% as the GDP threshold, rather than 75% which is currently used by the EU at NUTS2 level to define 'convergence' and 'competitiveness and employment' regions, reasonably clearly divided the regions of the EU-15 and post-socialist NMS into separate groups. Pakurár and Kovács (2008) had demonstrated major differences in the characteristics of the rural labour market of the two types of region.

Thus the RuralJobs typology addresses all three RuralJobs hypotheses and in so doing allows the potential for rural employment creation in different parts of the EU to be contrasted in the context both of urban-rural relationships and sustainable regional development strategies. As a contribution to the current debate on the shape of EU rural and regional development strategies for the period 2014-2020, this paper presents the results of this analysis.

**Methodology**

Case study research on current employment patterns and opportunities for, and constraints on, rural economic diversification was conducted in five contrasting NUTS2 regions across the EU. The research covered the following 'types' of region: 'high GDP - urban - accessible' and 'high GDP - intermediate - accessible' (UK); 'high GDP - predominantly rural - accessible' and 'high GDP - predominantly rural - remote' (France); 'low GDP - intermediate - accessible' (Bulgaria); 'low GDP - predominantly rural - accessible' and 'low GDP - predominantly rural - remote' (Hungary); and 'low GDP - predominantly rural - remote' (Romania). Thus all six most common 'types' of rural region were included in the research.

In order to examine the interaction between different types of rural area and the evolution of labour markets, travel to work areas and changing work patterns (as specified in the call for project proposals), 'labour market' or 'employment' areas (LMA) were used for the case study research. Remarkably, in most countries represented in the research, evidence was available which allowed LMAs to be defined, as follows: 'Travel to Work Areas' (TTWA) in the UK (Bond and Coombes, 2007); 'Local Labour Systems' (LLS) in Hungary (Radvánszki and Sütő, 2007); and 'agglomeration areas' in Bulgaria (Anon., 2007). In France, a 'Pays' is the result of a collective bottom-up approach with regional approval of its boundary. Only in Romania was it necessary to use an administrative territory (a NUTS3 region) as a case study area.

The evidence base for the research consisted of (a) information gathered from the interviews with local actors/key experts, (b) quantitative data sets and (c) previously published (mainly local) studies. In each case study area, a SWOT analysis of rural employment potential was conducted from the results of the field research. Further details of the SWOT analysis methodology are given in Fieldsend and Kerekes (in press).

**Results**

The NUTS2 regions in which the RuralJobs case studies were located are shown in Figure 1. A description of each region, based on the RuralJobs data analysis, is presented below and the components of the SWOT analyses which directly relate to accessibility of rural areas to urban centres are summarised.

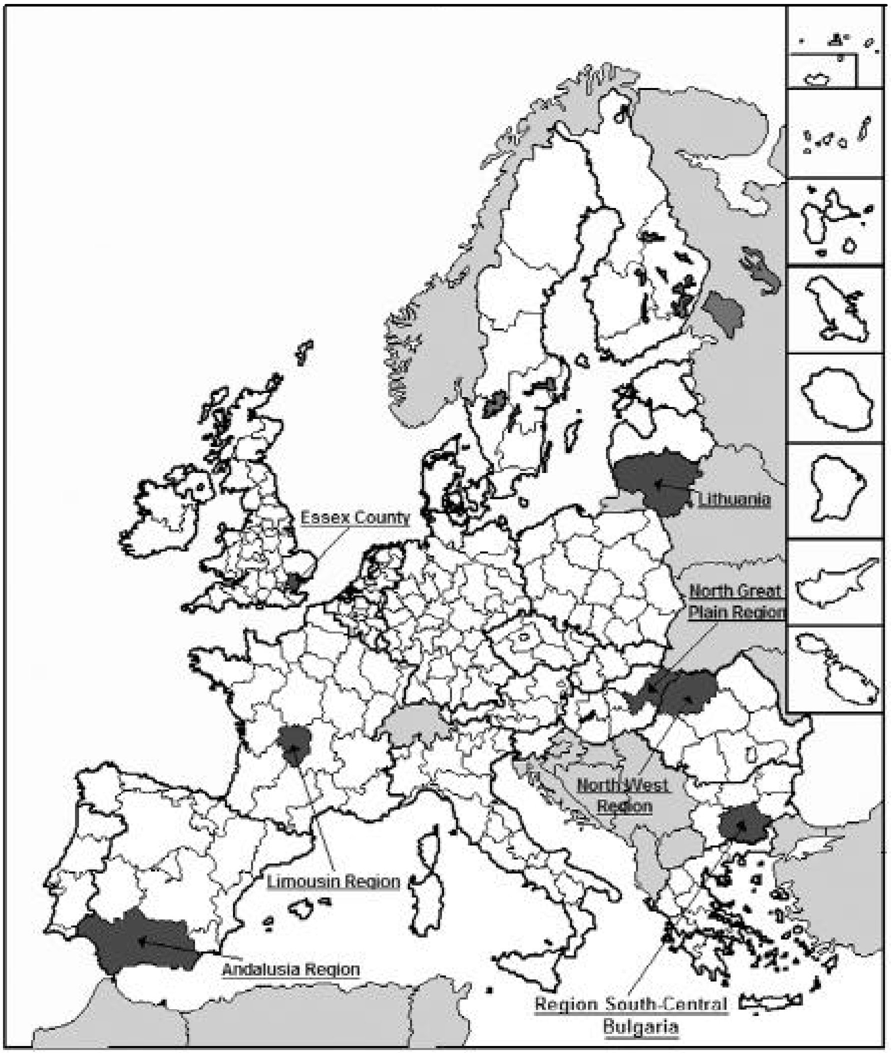


**Figure 1. NUTS2 regions included in the RuralJobs research. The case studies described in this paper were located in all of these regions except Andalusia Region and Lithuania.**

***The Chelmsford and Braintree TTWA, Essex, UK***

The Chelmsford and Braintree 'Travel to Work Area' (TTWA) is defined as a single labour market by Bond and Coombes (2007). In 2001 the TTWA had a population of 348,677, and it covers an area of 1313 km$^2$. It is located close to London (ca. 35 minutes from Chelmsford by train) and includes five towns, ranging from Chelmsford (population 97,451) to Halstead (population 10,000). Rural areas account for 37.7% of the population and 87.8% of the area. The TTWA is defined as 'high GDP - intermediate - accessible' in the RuralJobs typology as 100% of the population can access urban areas by car in 45 minutes or less. The population of the rural and urban areas increased by 6.2% and 5.0% respectively between 2001 and 2007 as did the percentage of people aged 65+, reaching 22.0% in rural areas and 17.2% in towns. The economic prosperity of rural and urban residents is similar and the mean number of cars in rural households was higher in rural areas (0.88 c.f. 0.81).

***Thames Gateway South Essex, Essex, UK***

Although the Thames Gateway South Essex (TGSE) sub-region is split between two 'Travel to Work Areas' (Bond and Coombes 2007), the territory is designated by the UK Government as a 'National Growth Area' and treated as a single entity. It is located on the north bank of the estuary of the River Thames and very close to London. It has just 38,095 rural residents out of a population of 633,687 and is dominated by the Southend-on-Sea urban area (pop. 266,749). TGSE covers 530 km$^2$ and although it is defined by RuralJobs as 'predominantly urban - accessible - developed', settlements of 10,000 or more cover less than 30% of the land surface. Even so, rural areas are feeling increasing pressures related to urbanisation. Rural land is used mostly for farming (arable and grassland), country parks and wildlife reserves.

***Pays de Tulle, région Limousin, France***

Pays de Tulle (PdT) lies entirely within the Tulle 'employment zone' (EZ) and, with a population in 2006 of 49,789 and an area of 1253 km$^2$, is defined by RuralJobs as 'high GDP - predominantly rural - accessible'. Even so, its only town, Tulle (for which PdT serves as a catchment area), has just 15,734 residents; Brive-la-Gaillarde (population 50,009) and Limoges (population 136,539) lie outside PdT. Two out of three people live in a municipality with less than 150 inhabitants $km^{-2}$. The population of PdT fell between 1962 and 1999, but there has since been a slight reversal in this trend, especially in rural areas surrounding Tulle, mainly owing to the in-migration of older people (the 65+ age group now makes up over 26% of the population); the population is ageing as young workers are still departing for more attractive centres. The motorisation rate in rural areas is higher than in Tulle (715 c.f. 474 vehicles per 1000 residents).

***Pays de Guéret, région Limousin, France***

Pays de Guéret (PdG) approximates to the eastern half of the Guéret EZ and is a ‘high GDP - predominantly rural - remote’ region. It covers 938 $km^2$ and in 1996 had a population of 37,540, of which two out of three lived in a municipality with less than 150 inhabitants $km^{-2}$ and 13,789 lived in the town of Guéret. It is estimated that over 97% of the territory is rural and that no part of PdG is located less than 50 minutes by car from Limoges. Since 1999 the urban and rural populations have stabilised after a period of decline as the slightly positive (+0.5%) annual migration balance offset the negative natural balance (-0.5%). Overall, the population is ageing: nearly 27% of the population is aged 65+. Areas of ageing population are concentrated in the north of PdG while younger, working age people live in the Guéret area or close to the main N145 road.

***Pazardjik ‘agglomeration area’ (AA), Pazardjik Oblast, Bulgaria***

The case study area, with a population in 2007 of 198,055 and covering 1907 $km^2$, consists of the six LAU1 municipalities in central Pazardjik Oblast. The main towns are Pazardjik (pop. 118,561), Peshara (21,653) and Septemvry (8,778). The case study area is defined as ‘low GDP - intermediate - accessible’ as 45.4% of the population live in rural LAU2 regions. Since 2000 the population has declined on average by 3.4%, but in the villages the average decrease was almost 5% (c.f. 2.5% in the towns) and in Belerovo municipality was 6.5%. In 2007, 57% of the rural population was of working age (c.f. 64% in the towns), up from 53% in 2000 and 28% was over working age (c.f. 19% in the towns), down from 31% in 2000. The number of people under working age is declining and the population is ageing. Rural natural population balance in 2007 was -4.6% (c.f.

0.1% in the towns). 8-10% of the working age population is working abroad but some retirees have returned to rural areas to gain an income from farming.

***Hajdúszoboszló LLS, North Gt. Plain Region, Hungary***

The case study area, which actually consists of Hajdúszoboszló LLS and two neighbouring villages, covers 768 km² and in 2007 had a population of 43,691, of which 23,800 lived in Hajdúszoboszló. It is defined as 'low GDP - predominantly rural - accessible' as the density of all LAU2 regions is less than 150 persons km$^{-2}$ and 100% of the residents can access the city of Debrecen (population 207,270) by car in less than 45 minutes. Between 2001 and 2007 the population remained declined slightly, as did the percentage of working age (68.5% in 2007 c.f. 68.1% in 2001) but the percentage of older people increased (from 14.0% to 15.7%) and that of younger people declined (18.0% to 15.8%). Both the migration and natural balance (the latter particularly in Hajdúszoboszló) have been negative since the 1990s. 2007 motorisation rates were comparable to the regional average of 260 cars per 1000 residents, c.f. 190 in 2001.

***Karcag LLS, North Gt. Plain Region, Hungary***

This case study area consists of Karcag LLS and two neighbouring villages. It covers 877 km² and in 2007 had a population of 46,170, of which 21,824 lived in Karcag and 12,224 lived in Kisújszállás. It is defined as 'low GDP - predominantly rural - remote' as the density of all LAU2 regions is less than 150 persons km$^{-2}$ and only around 40% of the residents can reach the city of Szolnok (population 75,474) by car in less than 45 minutes. Both the natural and migration balance have contributed to a 6% decline in the population (affecting almost all settlements) since 2001. Roma account for 8% of the population (13% in Karcag) and many are unskilled, long-term unemployed. The percentage of working age increased from 65.9% in 2001 to 68.1% in 2007 but the percentage of young people declined (from 19.2% to 16.8%). 2007 motorisation rates were substantially below the regional average of 242 cars per 1000 residents.

***Bistriţa-Năsăud county, North West Region, Romania***

Bistriţa-Năsăud county area covers an area of 5355 km² and in 2009 had a population of 317,205, of which 119,334 lived in rural areas. The urban centres and (2009) populations are Bistriţa (84,471), Beclean (11,574), Năsăud (10,906) and Sângeorz Băi (10,912). As less than 50% of the rural population can access Bistriţa (or any other major city) by car in 45 minutes or less it is defined as 'low GDP - predominantly rural - remote' in the RuralJobs typology. The towns are located in the centre of the county while the NE (mountain) and SW (hilly) areas are entirely rural. The rural population declined by 1.4% between 2002 and 2007 while the urban population increased by 1.0%. Rural society is both elderly and ageing: 65.6% of the rural population was of working age in 2008, compared to 63.1% in 2002, and 76.7% in towns in 2008. International migration is important, but there are no reliable registered figures on its extent. In 2008 the number of cars per household was 0.36 in urban and 0.16 in rural areas.

***Components of the SWOT analyses which directly relate to accessibility***

'*Good accessibility to/from major markets and service centres*' (by road, rail, air and sea) is a Strength in the Chelmsford and Braintree TTWA, as are '*Good service links*', '*Close proximity to industry and markets*' and '*Good transport links*' in Thames Gateway South Essex. Here, '*Links with industry*' is an Opportunity although '*Urbanisation*' is a Threat. In Pays de Tulle '*Proximity of Brive-la-Gaillarde*', reputed to be more dynamic, is an Opportunity together with '*Infrastructures to leverage the economy and employment*' (including Brive-Lille high-speed train, high-speed line to Limoges, Brive Airport), which is linked to the Strength '*Quality of communication infrastructures*' (road and air transport). A Weakness is that '*Aid for regional purposes is concentrated along the motorways*' which accentuates the disadvantages of the rural areas which are not close to major roads. '*Genial geographic and transport location*' and '*Relatively higher density of road infrastructure and networks compared to other parts of the country*' are Strengths in Pazardjik AA. A Strength in Hajdúszoboszló LLS is '*Good accessibility and infrastructural condition of the settlements*'. Thus all 'accessible' case study areas recognise the value of accessibility for rural employment.

Despite being 'remote', '*Easy (transport) access to the area*' is a Strength in Pays de Guéret although '*Capture of purchasing power and business by neighbouring centres*' (Montluçon (more dynamic), La Souterraine (more accessible)) is considered to be a Threat. In Karcag LLS a Weakness is that '*There are several settlements of difficult access in the area, the infrastructural conditions are weak*'.

In the NMS pilot areas, infrastructure improvements are an Opportunity for job creation, as follows: '*Significant resource which is available for amelioration and completion of the road infrastructure*' in Pazardjik AA (where a Weakness is '*The road infrastructure at 3 and 4 classes is in a despicable condition*'), '*Infrastructural development*' in Hajdúszoboszló LLS, '*Infrastructural and economic development*' in Karcag LLS and '*EU and national funds for the improvement of physical infrastructure*' (roads, utilities, etc.) in Bistriţa-Năsăud county where '*Inadequate physical infrastructure*' is a Weakness. '*Poor rural transport infrastructure*' (including roads) is a Weakness in the Chelmsford and Braintree TTWA; although the current provision is clearly much better than in the NMS, higher demands are placed upon it leading to problems such as traffic congestion.

## Discussion

### *Accessibility, remoteness and urban v. rural*

By coincidence, perhaps, there was a consensus amongst the case study areas in Bulgaria, France, Romania and the UK that rural areas were composed of the territory outside settlements of 9,000-10,000 people or more. By contrast, in Hungary, Hajdúszoboszló (pop. 23,800) and Karcag (pop. 21,824) were considered by RuralJobs to be rural (although the North Great Plain Regional Operational Programme (NGPOP, 2006) also uses a threshold of a daytime population of 10,000 to define urban and rural areas). In Karcag LLS, defined as entirely rural, only 26% of residents live in settlements of less than 12,000 people.

The link between 'accessibility' and settlements of 50,000 or more requires careful interpretation. The following 'accessible' case study areas included settlements of 50,000 or more: Chelmsford and Braintree TTWA (Chelmsford, pop. 99,962) Thames Gateway South Essex (Southend-on-Sea urban area (pop. 270,000) and others) and Pazardjik AA (Pazardjik, pop. 86,744). Bistriţa-Năsăud county also contains a large population centre (Bistriţa, pop. 83,571). This case study area was defined by RuralJobs as 'remote' on the basis that less than 50% of the *rural* population can access the city by car in 45 minutes or less. In fact, 67% (i.e. approx. 212,000 people) of the population lives within 30 km of the city. It should be noted, however, that the RuralJobs research was conducted in the 'remote' northern (mountainous) and southern (hilly) parts of the county. In four case study areas, therefore, there is a significant integration of the labour market between the rural areas and the urban centres of 50,000 or more.

By contrast, the largest settlement in the 'accessible' case study area of Pays de Tulle is Tulle and in Hajdúszoboszló LLS is Hajdúszoboszló. Although 'accessible' to Brive-la-Gaillarde, almost 87% of the active population living in the Tulle employment area work in the employment area. Tulle is a major employment centre: its jobs density (number of local jobs per resident of working age, for example see Hastings, 2003) is 1.87 compared to 0.71 in Pays de Tulle as a whole. Similarly, Hajdúszoboszló LLS is bordered on three sides by the much larger Debrecen LLS centred on the city of Debrecen. Thus, in both cases, towns smaller than the RuralJobs typology threshold of 50,000 are strong employment centres for their rural hinterlands. In Tulle, the main reason is the high level of public sector employment there, while Hajdúszoboszló is the most important spa area in Eastern Central Europe. The latter may be reinforced by the fact that commuting the fairly short distance to Debrecen is described as "tiring", which may be a cultural point or may reflect the relatively poor standard of the transport infrastructure in the case study area.

While the two other 'remote' case study areas, Pays de Guéret (France) and Karcag LLS (Hungary), differ from the 'accessible' case study areas in those countries in that the average driving time to the closest city of 50,000 inhabitants or more exceeds 45 minutes, they are otherwise similar in being centred on medium-sized settlements, namely Guéret and Karcag.

This overview confirms the importance to policy of the potential significance of medium-sized settlements as centres of employment (and services such as financial services, healthcare and secondary school education) for their rural hinterlands, and also the inappropriateness of a simple urban-rural divide. This is not a new finding. In the UK, for example, the potential of 'market towns', defined by their capacity to act as a focal point for trade and services for the surrounding countryside, and having populations approximately in the range from 2,000 to 20,000, (CA, 2003), has long been recognised (e.g. Courtney and Errington, 2000, Courtney et al. 2007). Their importance is emphasised in many strategies such as the current North Great Plain Regional Operational Programme in Hungary, and in the UK the 'Market Towns Initiative' was seen as good practice (Fieldsend and Boone, 2007). CA (2004) used the concept of 'settlements in the rural domain' for those with populations under 10,000. The RuralJobs research cannot elaborate extensively on present knowledge on this topic, but it may be appropriate to describe settlements under this threshold as 'small' and those above it as 'medium-sized' population centres in the 'rural domain'. A similar threshold has been used elsewhere, for example by van Leeuwen and Nijkamp (2004) in the Netherlands.

Where the number of jobs in a rural territory is insufficient, the working age population may respond by commuting to urban centres. In this case, high residence-based rural employment rates may thus conceal a serious lack of rural jobs, as measured by jobs density. Commuting is closely associated (although not inextricably linked) with counter-urbanisation, the demographic and social process whereby people move from urban areas to rural areas. Thus with counter-urbanisation the rural area is the place of residence while the urban centre is the place of economic activity.

Commuting is normally only a solution for those who live in 'accessible' rural areas (i.e. those who live in a labour market area which includes a population centre of significant size, such as a market town or a city) and who are mobile and/or can afford the cost of travel. The RuralJobs research shows that whilst in the EU-15 pilot areas car ownership (motorisation rate) tends to be higher in rural areas than in towns, in the NMS the opposite is the case. In the latter, travel costs as a percentage of salaries tends to be higher, and infrastructure tends to be poorer. Thus, the ability of rural residents in NMS to access jobs by (daily) commuting tends to be lower. However, where the intrinsic ability of rural areas to support employment is low, such as in the Pazardjik AA and Bistriţa-Năsăud county, commuting can help to maintain their economic viability and therefore population levels.

***Management of rural employment policy and funding streams in a regional context***

The RuralJobs research has described the considerable potential contribution of EU rural areas in general to regional employment and economic prosperity based on the sustainable exploitation of natural capital

(Fieldsend and Kerekes, in press). The list of rural growth sectors identified by RuralJobs is similar to that provided by CRC (2010): low carbon economy including environmental and renewable technologies; Food and drink; Tourism; Business and professional services; Digital and creative industries; Health and social care sectors; ICT; Construction; Retail and Advanced manufacturing. The relative importance of the different sectors to rural job creation varies widely in different rural areas across the EU, but natural capital is a common theme. At the same time, rural job creation depends upon product and process innovation linked with skills development of the workforce. Many innovative initiatives are related to the environment, including bioenergy, showing them to be emergent sectors of innovation (Rapido, 2008). Yet Hepworth et al. (2004) stated "Regional economic strategies suffer from 'double vision': a competitive knowledge economy vision for urban areas and a sustainable community vision for rural areas – what is needed is a unified regional vision of the knowledge economy and sustainable development".

The 'city regions' approach to economic development (see, for example, http://www.rce.org.uk/?P=HOME) assumes that larger urban sub-regions, cities and their hinterlands will disproportionately drive economic growth. Rural areas within these regions can therefore be expected to benefit. However, if implemented wrongly, an urban-focused approach such as this can push knowledge-based employment into the towns and neglect the potential economic contribution of rural areas. Indeed it could precipitate a 'race to the bottom' by excessively targeting funding at urban centres and contributing to the economic and social decline of the rural hinterlands manifested in trends such as ageing populations. This could be a particular concern in the NMS where, as previously noted, motorisation rate, and therefore the ability to commute, is lower. To comply with the priorities of the EU's Europe 2020 strategy, namely smart, sustainable and inclusive growth (EC, 2010), regional development strategies should include a distinct rural component which recognises the potential contribution of natural capital, and therefore rural areas, to providing employment and in so doing achieving a competitive regional knowledge economy.

The need identified by Marsden (1999) for a more integrated approach to rural development (employment) policy and funding remains, as the agenda must move beyond creating employment only in the food, farming and tourism sectors. Even if a case can be made for a separate Rural Development Fund after 2013, the development of the Programme must be much more closely coordinated with those of EU Structural Funds and other funding instruments. The funding programmes themselves need to be better aligned with each other (and with national funding) to increase their impact. This does not mean targeting programmes even more precisely, such as via a menu approach, as this can create inflexibility and funding gaps. Also they should be investment orientated and objective-focused rather than subsidy orientated and beneficiary-focused so as to maximise their favourable impacts on the region as a whole, including with respect to employment.

As part of the coordination agenda, Rural Development and Structural Funds should be managed at the same geographical level. In line with the principle of subsidiarity, Member States are best placed to select the most appropriate level, although it may be noted that Structural Funds are frequently managed at NUTS2 level. The increasing integration of 'urban' and 'rural' economies strengthens the case for 'mainstreaming' rural job creation into a single regional programme. For this to be successful, such programmes should be designed from the start with rural in mind. 'Rural proofing' applied to an urban-focused programme as an afterthought, using a 'tick-box' approach, is not sufficient. Finally, whilst management of all funding in a region by a single body is an option (such as in England by the (NUTS1) Regional Development Agencies), management of different funds by separate organisations working in close partnership may be an approach preferred by some Member States.

The RuralJobs research identified several weaknesses in the evidence base required to ensure that rural employment creation programmes are as effective as possible. For example, more research is needed to formulate a definition of LMAs which can be applied across the EU. The concept of a self-contained LMA is one in which all commuting occurs within the boundary of the area. Although in practice it is not possible to divide territories into entirely separate LMAs as commuting patterns are too diffuse, leading to elements of subjectivity in the methodology (including defining the appropriate minimum and maximum thresholds for numbers of jobs and workers), LMAs have been invaluable to RuralJobs and have also been used by other researchers (e.g. by Simmie and Martin (2010) in their work on economic resilience of regions). By contrast, EU-wide definitions of ‘urban’ and ‘rural’ would not be helpful. In fact, the rather arbitrary definitions officially adopted in some NMS and used for classifying territorial data have been unhelpful to the RuralJobs research.

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# Romanian Entrepreneurship in International View

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**Abstract**

The aim of this article is to identify Romania's place among the 71 countries, which participated in the Global Entrepreneurship Monitor project in at least one year between 2002-2009 time period, by entrepreneurship and economic development level. The study is based on individual and institutional variables, which are the main components of the Global Entrepreneurship and Development Index.

**Keywords:** Global Entrepreneurship and Development Index, entrepreneurial aspirations, entrepreneurial activity, entrepreneurial attitudes, Global Entrepreneurship Monitor.

**JEL Classification:** L26, O10, O57

## Introduction

Recently, the relation between entrepreneurship and economic development appears to be a widely treated subject in the literature. According to Naudé (2008) despite the progress, entrepreneurship in economic development remains a relatively under-researched phenomenon. Acemoglu and Johnson (2005) affirmed that the economic development is strengthened by the productive entrepreneurial activity.

There are some research projects, which are actively involved in measuring the quality and quantity of entrepreneurship across countries and over time (i.e., Global Entrepreneurship Monitor, World Bank, The Heritage Foundation and the World Economic Forum projects).

Global Entrepreneurship Monitor (GEM) is a large-scale research program launched in 1997 by leading researchers in the field of entrepreneurship at London Business School and Babson College. The main aim

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of GEM research is to study the complex relationship between entrepreneurship and economic growth, to measure the level of entrepreneurial activity between countries, to uncover factors determining the levels of entrepreneurial activity and to identify policies which may stimulate the level of entrepreneurial activity. GEM, as a research program that focuses on a major driver of economic growth, on entrepreneurship, admits the widely acknowledged phenomena that entrepreneurship is one of the most important forces shaping the changes in the economic landscape.

Acs and Szerb developed in 2009 the Global Entrepreneurship and Development Index (GEDI), which offers a measure of the quality and quantity of the business formation process in 71 countries[6] in the world. This index captures the contextual feature of entrepreneurship by focusing on entrepreneurial attitudes, entrepreneurial activity and entrepreneurial aspirations.

In this article we present a country level interpretation of Acs and Szerb's GEDI index and its three pillars (entrepreneurial activity, entrepreneurial aspiration, and entrepreneurial attitudes) regarding the Romanian entrepreneurship in international comparison.

**Methodology and data**

The GEDI index components are based on individual level or institutional level variables. All individual level variables are from the GEM Adult Population Survey. The institutional variables are obtained from various sources, like the World Economic Forum, The Heritage Foundation, Coface, UNESCO, etc. All pillars or indicators were calculated from the variables by multiplying the individual variable with the proper institutional variable. The indicators are the basic building blocks of the three sub-indexes: entrepreneurial attitudes, entrepreneurial activities, and entrepreneurial aspirations. The Penalty for Bottleneck[7] method is used to calculate the three sub-indexes from the indicators. Finally, the GEDI is simply the average of the three sub-indexes (for details see Appendix 2).

[6] These countries participated in the Global Entrepreneurship Monitor project at least one year between 2002-2009 (see Appendix 1).

[7] The Penalty for Bottleneck takes into account the weakest pillar value of a particular sub-index and penalizes for the differences between pillars.

The entrepreneurial attitude (ATT) sub-index aims to identify entrepreneurial attitudes associated with the entrepreneurship-related behaviour of a country's population. This sub-index takes into consideration the following indicators: opportunity perceptions, start-up skills, non-fear of failure, networking and cultural support.

The entrepreneurial activity (ACT) sub-index is principally concerned with measuring high growth potential start-up activity based on opportunity start-up, technology sector, quality of human resources, competition.

The entrepreneurial aspiration (ASP) sub-index refers to the distinctive, qualitative, strategy related nature of entrepreneurial activity based on the novelty of the product and the technology, high growth aspirations, internationalisation (which takes into consideration the share of foreign customers), and risk capital.

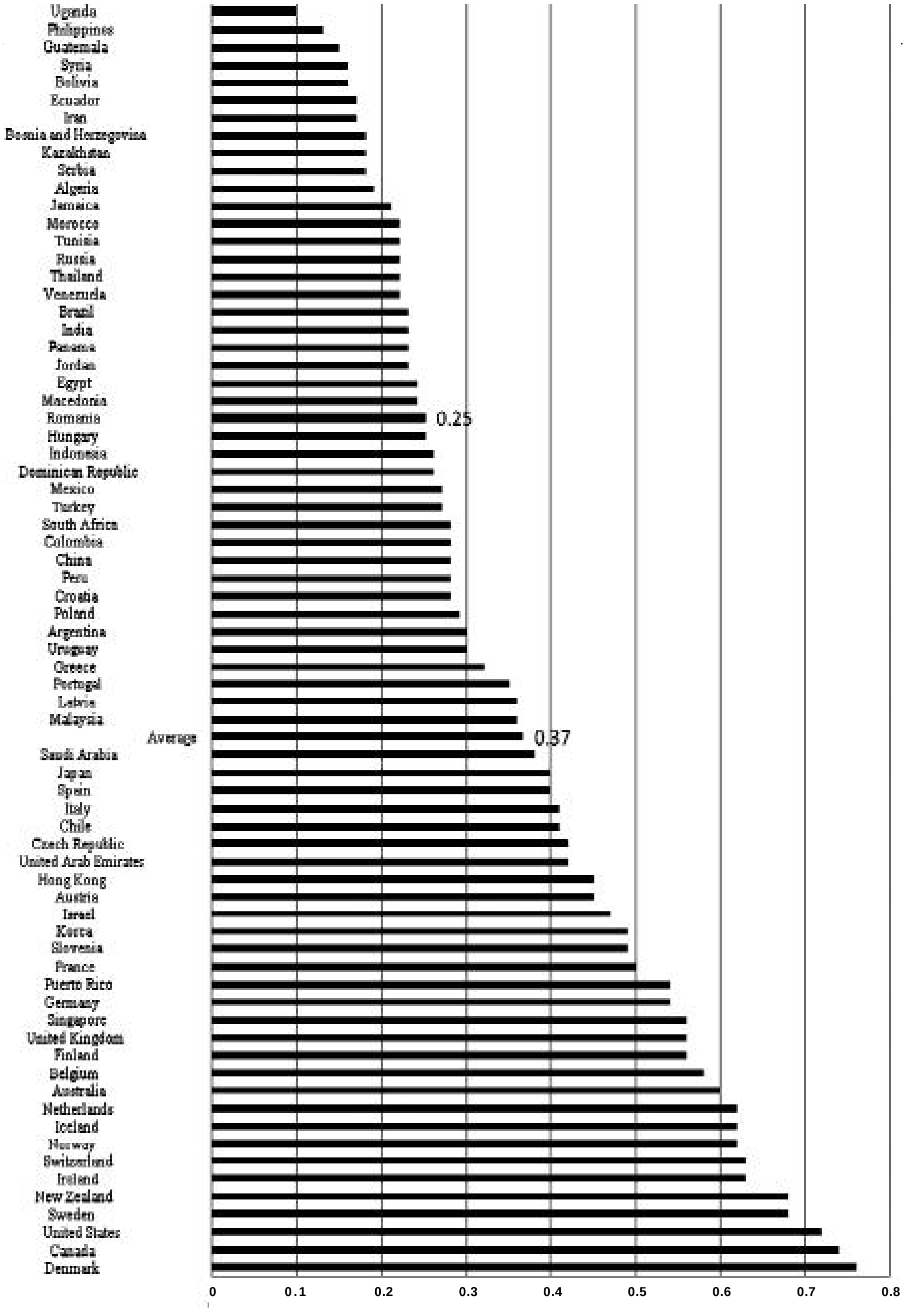
The data is based on the pooled data of 71 countries in the 2002-2008 time periods. Not all the countries participated in each year of the GEM survey. Romania's position is analysed based on the 2007 and 2008 data.

**Global Entrepreneurship and Development Index in Romania**

The values of the GEDI by countries can be seen in Figure 1. According to this figure, Romania ranks 48$^{th}$, with 0.25 points. Denmark has the highest GEDI value, more than three times higher than Romania. The value registered in Romania is lower than the GEDI average (0.37) of the analysed GEM participating countries.

A more proper analysis is to compare Romania's position to similarly developed countries. The highest ranked efficiency-driven economy[8],

[8] The Global Entrepreneurship Monitor Global Reports (Bosma et al., 2009, p.4; Bosma & Levie, 2010, p.5) classify the participating countries in three groups which are considered to be relevant to entrepreneurship in relation to economic development, on basis of the Global Competitiveness Reports: factor-driven economies, efficiency-driven economies and innovation-driven economies. The efficiency-driven economies begin to develop more efficient production processes and increase product quality than the factor-driven economies. In the efficiency-driven economies competitiveness is increasingly driven by higher education and training, efficient goods markets, well-functioning labor markets, sophisticated financial markets, a large domestic and/or foreign market, and the ability to harness the benefits of existing technologies. The efficiency-driven economies are: Argentina, Bosnia and Herzegovina, Brazil, Chile, China, Colombia, Croatia, Dominican Republic, Ecuador, Hungary, Iran, Jordan, Latvia, Macedonia, Malaysia, Mexico, Panama, Peru, Poland, Romania, Russia, Serbia, South-Africa, Thailand, Tunisia, Turkey, and Uruguay.



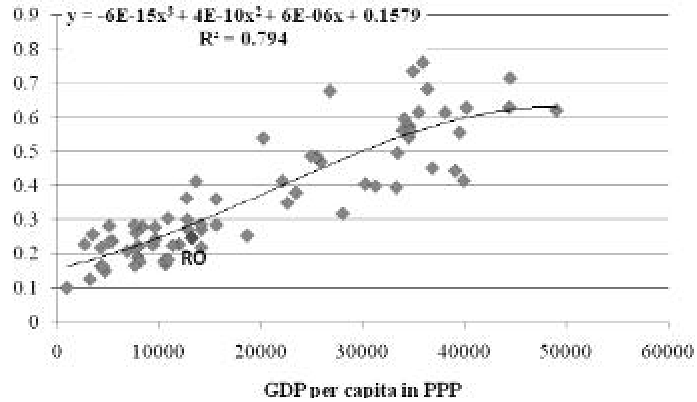

*Source: www.gemconsortium.org*

**Figure 1. Global Entrepreneurship Development Index (GEDI) by country**

Chile, has 0.41 GEDI value, which is 1.6 times higher than Romania's. The lowest value from these economies is reached by Ecuador (0.17). Of the 27 efficiency-driven economies, Romania is 16th, still in the second half. Among the transitional Central and Eastern European countries, Romania is in the middle position. Only three countries, Poland, Croatia, and Hungary, overtake Romania, Hungary by a very small margin. The other CEE countries, Macedonia, Russia, Serbia, and Bosnia and Herzegovina, are behind Romania.

The next four figures present Romania's relative position, not only in the GEDI, but also in the three sub-indexes in terms of GDP per capita. The curves represent the development implied trend line of the GEDI index and the three sub-indexes.

In case of Figure 2 the trend line[9] is based on a third-degree polynomial fitting. Romania is situated below the trend line, which means that the Romanian entrepreneurial performance is relatively unfavourable.




*Source: Calculations based on Acs, Z.A. & Szerb, L. methodology*

**Figure 2. Global Entrepreneurship Development Index by GDP per Capita**

Romania is somewhat below the development implied trend line in all four cases. Romania ranks 53rd in the Entrepreneurial Attitudes Sub-index, 44th in the Entrepreneurial Activity Sub-index, and 47th in the Entrepreneurial Aspiration Sub-index among the 71 GEM participating countries (see Table 1).

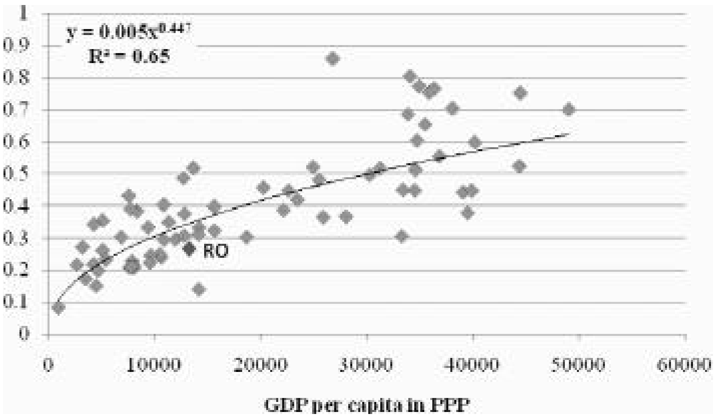
[9] If a country's position is below the trend line, it means it has a lower level of performance of that particular factor than implied by its development trend. A position above the trend line means a relatively favourable entrepreneurial performance.

**Table 1. Romania's ranking among GEM participating countries by GEDI and the three sub-indexes**

| | GEDI | ATT | ACT | ASP |
|---|---|---|---|---|
| Global (71 countries) | 48 | 53 | 44 | 47 |
| Efficiency-driven economies (27 countries) | 16 | 18 | 11 | 14 |

*Source: Own calculations based on GEIbynation.xls*[10]

Figure 3 presents the Entrepreneurial Attitudes Sub-index by GDP per capita. In this case the trend line is based on a power regression. The opportunity perception is the weakest between the Entrepreneurial Attitudes Sub-index components, which has a negative influence on the other four components of the sub-index.




*Source: Calculations based on Acs, Z.A. & Szerb, L. methodology*

**Figure 3. Entrepreneurial Attitudes Sub-index by GDP per Capita**

Romanian entrepreneurs have a low level of the skills needed for a successful start-up, the vital cultural recognition and support of entrepreneurs is also missing. The difference from the trend line is the greatest in the case of Entrepreneurial Attitudes Sub-index, which can be seen in Figure 3. At the same time, the other two attitude pillars, the level of networking and the risk tolerance, are acceptable, as Table 2 shows it.

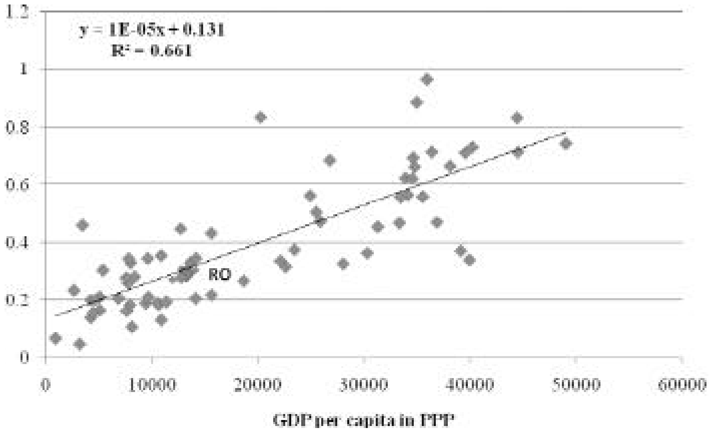
[10] www.gemconsortium.org/Members area

**Table 2. Romania's ranking among GEM participating countries by the components of the Entrepreneurial Attitudes Sub-index**

| | Opportunity perception | Start-up skills | Non fear of failure | Net-working | Cultural support |
|---|---|---|---|---|---|
| Global (71 countries) | 63 | 58 | 40 | 32 | 56 |
| Efficiency-driven economies (27 countries) | 23 | 23 | 9 | 6 | 21 |

*Source: Own calculations based on GEIbynation.xls*

Also, we can observe on the figure below (Figure 4), that this difference is the least in case of the Entrepreneurial Activity Sub-index. The low level of technology sector start-ups limits the activity. Next to start-ups in the technology sector, the high level of competition is the weakest pillar of the activity. High competition means that Romanian start-ups mainly occur in sectors that already have many similar businesses.




*Source: Calculations based on Acs, Z.A. & Szerb, L. methodology*

**Figure 4. Entrepreneurial Activity Sub-index by GDP per Capita**

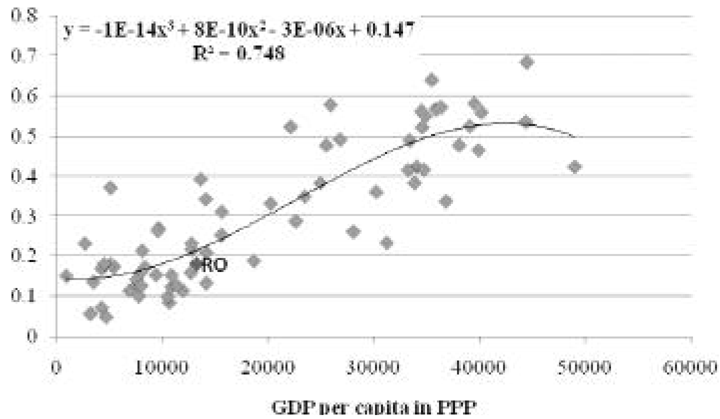
The strongest pillar value is the quality of human resources (which value is the highest among the efficiency-driven economies), meaning that entrepreneurs, who have at least a postsecondary education, start new start-ups and young businesses in Romania.

**Table 3. Romania's ranking among GEM participating countries by the components of the Entrepreneurial Activity Sub-index**

| | Opportunity start-up | Technology sector | Quality of human resource | Competition |
|---|---|---|---|---|
| Global (71 countries) | 43 | 59 | 11 | 56 |
| Efficiency-driven economies (27 countries) | 10 | 24 | 1 | 19 |

*Source: Own calculations based on GEIbynation.xls*

Romania's lowest sub-index value is in the Entrepreneurial Aspiration Sub-index, which means that the difference between Romania and the leading nations is the highest in case of the Entrepreneurial Aspiration Sub-index.




*Source: Calculations based on Acs, Z.A. & Szerb, L. methodology*

**Figure 5. Entrepreneurial Aspiration Sub-index by GDP per Capita**

The aspiration sub-index contains the most diverse value pillars. The application of new technology and the missing formal and informal venture capital are the two weakest performing pillars, not only in the Entrepreneurial Aspiration Sub-index but also in the whole system. The new technology component is the weakest among all GEM participating countries. The internationalisation is the strongest pillar, meaning that Romanian start-ups are open to export to international markets (3rd place among the efficiency-driven economies). The large number of Romanians working abroad probably fuels internationalisation. To improve Entrepreneurial Aspiration Sub-index, the product and technology innovation as well as the venture finance position should be strengthened.

**Table 4. Romania's ranking among GEM participating countries by the components of the Entrepreneurial Aspiration Sub-index**

| | New product | New tech | High growth | Internatio-nalisation | Risk capital |
|---|---|---|---|---|---|
| Global (71 countries) | 46 | 71 | 31 | 16 | 63 |
| Efficiency-driven economies (27 countries) | 15 | 27 | 9 | 3 | 23 |

*Source: Own calculations based on GEIbynation.xls*

**Conclusions**

Romania appears among the lowest 33 percentage of the entrepreneurial economies and ranks 48th by GEDI. It performs the worst on the Entrepreneurial Attitudes Sub-index. At the pillar level, Romania is strong in internationalisation, quality of human resources and networking, but weak in new technology, risk capital and opportunity perceptions. The improvement of opportunity recognition capabilities can be done through educational changes. The low ranking regarding the new technology usage is caused mainly by the lack of new technology-oriented individual initiatives. Informal venture capital is identified also as being problematic. Formal venture capital investment could be improved by further development of stock and capital markets.

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**Appendix 1. The GEM participating countries between 2002–2008 and the new countries in 2009** *(Source: www.gemconsortium.org)*

| Country | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|---|---|---|---|---|---|---|---|---|
| Algeria | | | | | | | | x |
| Argentina | x | x | x | x | x | x | x | |
| Australia | x | x | x | x | x | | | |
| Austria | | | | x | | x | | |
| Belgium | x | x | x | x | x | x | x | |
| Bolivia | | | | | | | x | |
| Bosnia&Her. | | | | | | | x | |
| Brazil | x | x | x | x | x | x | x | |
| Canada | x | x | x | x | x | | | |
| Chile | x | x | | x | x | x | x | |
| China | x | x | | x | x | x | | |
| Colombia | | | | | x | x | x | |
| Croatia | x | x | x | x | x | x | x | |
| Czech Republic | | | | | x | | | |
| Denmark | x | x | x | x | x | x | x | |
| Dominican Rep. | | | | | | x | x | |
| Ecuador | | | x | | | | x | |
| Egypt | | | | | | | x | |
| Finland | x | x | x | x | x | x | x | |
| France | x | x | x | x | x | x | x | |
| Germany | x | x | x | x | x | | x | |
| Greece | | x | x | x | x | x | x | |
| Guatemala | | | | | | | | x |
| Hong-Kong | x | x | x | | | x | | |
| Hungary | x | | x | x | x | x | x | |
| Iceland | x | x | x | x | x | x | x | |
| India | x | | | | x | x | x | |
| Indonesia | | | | | x | | | |
| Iran | | | | | | | x | |
| Ireland | x | x | x | x | x | x | x | |
| Israel | x | | x | | | x | x | |
| Italy | x | x | x | x | x | x | x | |
| Jamaica | | | | x | x | | x | |
| Japan | | x | x | | x | x | x | |

| Country | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 |
|---|---|---|---|---|---|---|---|---|
| Jordan | | | | | | | | x |
| Kazakhstan | | | | | | x | | |
| Korea | x | | | | | | x | |
| Latvia | | | | x | x | x | x | |
| Macedonia | | | | | | | x | |
| Malaysia | | | | | x | | | |
| Mexico | x | | | x | x | | x | |
| Morocco | | | | | | | | x |
| Netherlands | x | x | x | x | x | x | x | |
| New Zealand | x | x | x | x | | | | |
| Norway | x | x | x | x | x | x | x | |
| Panama | | | | | | | | x |
| Peru | | | x | | x | x | x | |
| Philippines | | | | | x | | | |
| Poland | x | | x | | | | | |
| Portugal | | | x | | | x | | |
| Puerto Rico | | | | | | x | | |
| Romania | | | | | | x | x | |
| Russia | x | | | | x | x | x | |
| Saudi Arabia | | | | | | | | x |
| Serbia | | | | | | x | x | |
| Singapore | x | x | x | x | x | | | |
| Slovenia | x | x | x | x | x | x | x | |
| South Africa | x | x | x | x | x | | x | |
| Spain | x | x | x | x | x | x | x | |
| Sweden | x | x | x | x | x | x | | |
| Switzerland | x | x | | x | | x | | |
| Syria | | | | | | | | x |
| Thailand | x | | | x | x | x | | |
| Tunisia | | | | | | | | x |
| Turkey | | | | | x | x | x | |
| Uganda | | x | x | | | | | |
| United Arab Em. | | | | | x | x | | |
| United Kingdom | x | x | x | x | x | x | x | |
| United States | x | x | x | x | x | x | x | |
| Uruguay | | | | | x | x | x | |
| | | x | | x | | x | | |

**Appendix 2. The Global Entrepreneurship and Development Index and its components**

| Individual Variables | | Institutional Variables | | Pillars (Indicators) | Sub-Indexes | GEDI |
|---|---|---|---|---|---|---|
| Opportunity[11] | x | Marketagglom[12] | = | Opportunity perception | ATTITUDES | Global Entrepreneurship Development Index |
| Skill[13] | x | Educpostsec[14] | = | Startup skills | | |
| Nonfear[15] | x | Business risk[16] | = | Nonfear of failure | | |
| Knowent[17] | x | Internetusage[18] | = | Networking | | |
| Carstat[19] | x | Corruption[20] | = | Cultural support | | |
| Teaopport[21] | x | Freedom[22] | = | Opportunity startup | ACTIVITY | |
| Techsect[23] | x | Techabsorp[24] | = | Technology sector | | |
| Higheduc[25] | x | Stafftrain[26] | = | Quality of human resources | | |
| Compet[27] | x | Markdom[28] | = | Competition | | |
| Newp[29] | x | Gerd[30] | = | New product | ASPIRATION | |
| Newt[31] | x | Innov[32] | = | New tech | | |
| Gazelle[33] | x | Buss strategy[34] | = | High growth | | |
| Export[35] | x | Glob[36] | = | Internationalization | | |
| Infinv[37] | x | Ventcap[38] | = | Risk capital | | |

*Source: Acs, Z.J. and Szerb, L. (2010b: pp. 46–51)*

[11] The percentage of the 18-64 aged population recognizing good conditions to start business next 6 months in area he/she lives.
[12] The size of the market: a combined measure of the domestic market size and the urbanization that later measures the potential agglomeration effect.
[13] The percentage of the 18-64 aged population claiming to posses the required knowledge/skills to start business.
[14] Gross enrolment ratio in tertiary education.

[15] The percentage of the 18-64 aged population stating that the fear of failure would not prevent starting a business.

[16] The business climate rate reflects whether corporate financial information is available and reliable, whether the legal system provides efficient creditor protection, and whether a country's institutional framework is favorable to inter-company deals.

[17] The percentage of the 18-64 aged population knowing someone who started a business in the past 2 years.

[18] The number of internet users in a particular country per 100 inhabitants, 2008, except 2009 countries that are from 2009.

[19] The status and respect of entrepreneurs.

[20] The Corruption Perceptions Index (CPI) measures the perceived level of public-sector corruption in a country.

[21] Percentage of the opportunity-driven early-stage entrepreneurs (TEA).

[22] Business freedom is a quantitative measure of the ability to start, operate, and close a business that represents the overall burden of regulation, as well as the efficiency of government in the regulatory process.

[23] Percentage of the TEA businesses that are active in technology sectors (high or medium).

[24] Firm level technology absorption capability.

[25] Percentage of the TEA businesses owner/managers having participated over secondary education.

[26] The extent of staff training.

[27] Percentage of the TEA businesses started in those markets where not many businesses offer the same product.

[28] Extent of market dominance.

[29] Percentage of the TEA businesses offering products that are new to at least some of the customers.

[30] Gross domestic expenditure on Research & Development (GERD) as a percentage of GDP.

[31] Percentage of the TEA businesses using new technology that is less than 5 years old average (including 1 year).

[32] Innovation index points from GCI.

[33] Percentage of the TEA businesses having high job expectation average (over 10 more employees and 50% in 5 years).

[34] Refers to the ability of companies to pursue distinctive strategies, which involves differentiated positioning and innovative means of production and service delivery.

[35] Percentage of the TEA businesses where at least some customers are outside country (over 1%).

[36] A part of the Globalization Index measuring the economic dimension of globalization.

[37] The amount of informal investment.

[38] A measure of the venture capital availability.

# The Changing Role of Managerial Accounting and the Managerial Accounting Profession in Romania

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**Abstract**

In this article we discuss about the changing roles of managerial accounting and the managerial accounting profession. After analyzing the existing literature in the field we would like to identify (1) how the objectives and functions of managerial accounting changed over the last years; (2) a set of characteristics, skills and competences of yesterday's and today's management accountant. We would like to point out that through accounting professionals managerial accounting becomes a business partner or analyst for every organization. After the international review the next step of our research is to identify the way managerial accounting and the managerial accounting profession is perceived by Romanian researchers, academics and practitioners. Our research results are based on previous studies made by Romanian researchers and a questionnaire based survey made by us among accounting professionals in Romania.

**Keywords:** Managerial accounting, management accountant, accounting profession, skills, competences, Romania

**JEL Classification**: M4, M10, M49

## 1.Introduction

The change of management accounting and the changing roles of management accountants has dominated both the professional and academic accounting literature in recent years (Yazdifar&Tsamenyi, 2005). Researchers (Burns&Scapens, 2000; Pierce&O'Dea, 2003; Burns&Baldvinsdottir, 2005; Jarvenpaa, 2007) consider that hypercompetition and globalization are two phenomena that generate complexity in the business environment; they create turbulence and disorder in the competitive environment. Under these conditions companies around the world need to permanently update their products and services to fit the market's demands;

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they need sophisticated production processes, flexible internal processes to be able to react quickly to the changes of the environment. These phenomena leave their marks on the accounting systems and the way that financial and managerial accounting is organized.

Under these conditions managerial accounting has to undergo to a procedure of „*unlearning certain old operations*" (Albu, 2005), it has to give up its role of "*watchdog*" or "*scorekeeper*" (Jarvenpaa, 2007) having to learn new practices to become an active consultant of management and a permanent participant of the decision making process (Burns&Baldvinsdottir, 2005).

In Romania, changes generated by globalisation, the intensification of competition, technologies of production processes have penetrated more slowly, because of the economic-political context and the development of the economy. Due to the same motives, managerial accounting has had a slower evolution as well than it had on international level. In time, managerial accounting in Romania has met different approaches, goals and objectives. Managerial accounting professionals were seen more like *bean counters* or *accountants doing cost calculations* instead of advisors of management.

These changes encouraged us to engage in this research in the field of managerial accounting. Our objective is to present a general overview of managerial accounting and the managerial accounting profession both on international and national level in order to gain useful knowledge for researchers, academics and practitioners also.

## 2.Research methodology

In order to create a good research in the field of managerial accounting and in order to generate good and relevant knowledge researchers must follow a set of qualitative criteria. According to Lukka&Mouritsen (2002) this set of qualitative criteria consists of theory, testing and rigour. Theory is used, on one hand, not to obtain predictions but to gain understanding of certain phenomena, to understand and explain the actual knowledge, and on the other hand to identify new research objectives and to formulate new hypotheses. After this testing plays an important role in every research because the developed theories and hypotheses have to be tested, gained results have to be published in order to get feedback from other researchers, practitioners or public. Together, theory and testing, must be done with precision and seriousness.

The remainder of this paper is laid out as follows. The following two sections represent a brief review of the existing literature; it examines the theoretical perspectives of managerial accounting, the accounting profession, and the management accountant's role in today's tumultuous and often changing environment. The main objective is to present a summary of the antecedents, characteristics and consequences regarding the roles of management accountants, emphasizing that the roles of management accountants may be moving towards a "business partner" or "financial analyst" model.

After the international literature review we focus on the evolution, characteristics and objectives of managerial accounting in Romania. We try to identify the way managerial accounting and the managerial accounting profession is perceived by Romanian researchers, academics and practitioners based on a previous study of Albu (2006) and a questionnaire based survey made in 2010 by Volkan among accounting professionals.

In the end the conclusions are drawn in order to offer solutions to the gaps identified and to establish further research objectives and opportunities.

## 3. Past and present in managerial accounting

### *3.1. A brief literature review – international level*

During recent decade there have been intensive, academic and professional, debates on the changing role of managerial accounting. Over the years researchers and academics tried to build a better understanding of the contemporary roles and functions of managerial accounting.

According to Jarvenpaa (2007) the studies in the field of managerial accounting can be divided in three major categories: (1) classical studies about the roles of managerial accounting; (2) studies dealing with the current role change from different angles; (3) studies strictly related to managerial accounting and organizational change.

Simon (1978) conducted a classical study about the role of managerial accounting. In his opinion managers have the following expectations regarding management accounting: scorekeeping – capturing, recording, summarizing and reporting financial performance; attention directing – drawing the attention of managers and assisting them in the interpretation of business performance; and problem solving – identifying the best choice from a range of alternative actions. Similar studies were conducted by Mouritsen (1996), Burns&Scapens (2000) or Drury (2001). According to them managerial accounting is an important routine or set of routines (Burns&Scapens, 2000) aiming to support managers' decisions and to provide organizational accountability. Managerial accounting supports the planning process when choices are made and budgets are elaborated and it is also involved in the operational process when actual events are identified, measured and registered to provide economic feedback to managers and to assist them in controlling costs and improving the efficiency and effectiveness of operations (Drury, 2001).

The classical studies about managerial accounting were followed by those dealing with the current role change from different angles. The current social and business environments, structural changes and innovations, sophisticated information systems development induced companies to implement profound changes in their business-management models, their management instruments and their methods of managerial accounting (Guerreiro et al, 2006). Literature in this field (Ribeiro&Scapens, 2006; Jarvenpaa, 2007; Byrne&Pierce, 2007; Jarvenpaa, 2009) has pointed out the changing role of managerial accounting function, from being a scorekeeper or watchdog to being a business analyst, an active advisor of management in the decision making process. In their opinion managerial accounting has become more business oriented, involving relevant accounting systems, personal competences and overall business knowledge, personal and organizational desire. Moreover, new managerial accounting techniques such as activity based costing, strategic cost management, target costing, balanced scorecard, customer profitability analysis, modern financial and operational control systems and software packages enhanced the business orientation of managerial accounting.

The third category of studies identified are those who refer to managerial accounting and organizational change and organizational culture (Burns&Vaivio, 2001; Burns et al, 2003; Bhimani, 2003; Guerreiro et al, 2006). Researchers tried to reveal relationships between accounting systems and organizational culture; they studied how behavioral and cultural aspects or certain notional elements of organizational culture became embedded in the design of innovative management accounting systems. Guerreiro et al (2006) talks about the institutionalisation of managerial accounting. In their opinion managerial accounting provides an institutional basis for decision-making and for structuring the formation of beliefs and expectations of the different groups of people inside organization. Moreover, managerial accounting provides social coherence in organizational behavior and might play an important role in defining the rights held by groups of individuals (owners, founders, managers, workers) and can be used as a conflict mediator inside an organization.

### *3.2. A brief literature review – national level*

In Romania, managerial accounting has had a certain evolution, a little different and slower compared to the international evolution, as it has been strongly influenced by political and social regimes and the development of Romanian economy.

For a long period of time managerial accounting was seen by Romanian researchers and professionals as a flexible activity whose main objectives are knowing the costs of various business functions and activities; monitoring, analyzing and controlling production costs; planning and controlling the allocation of resources through budgets and other management tools (Olariu, 1977; Baciu&Dutia, 1981; Airinei, 1993; Manolescu, 1994). We note that the major concerns of the researchers are to propose theoretical and methodological solutions and procedures regarding costing; to develop technical aspects of cost accounting; to propose and develop cost calculation methods such as process costing, job-order costing or standard costing.

Others (Oprea&Caraiani, 1993; Matiş&Danciu, 1994; Ristea, 1995; Cristea, 1997; Dumbravă&Pop, 1997) consider that besides the calculation, analysis and control of costs; or besides budgeting, managerial accounting assures the analytical representation of a company's internal business processes; it is preoccupied with planning, evaluating and controlling the company's resources; processing, interpreting and providing useful information to managers in the decision making process improving the efficiency and effectiveness of internal business processes and operations.

After 2000 managerial accounting experienced a more modern approach. Romanian researchers and academics (Ionaşcu et al, 2003; Caraiani&Dumitrana, 2005; Albu&Albu, 2006; Diaconu, 2006; Albu&Udroiu,

2009; Volkan, 2008; Tabără, 2009) give increased attention to the international literature; they admit that the influence sphere of managerial accounting is much wider; it does not reduce only to cost calculation. In addition to traditional tasks and objectives identified, new goals of managerial accounting are identified: providing financial and non-financial information to management necessary to the decision making process; integrating financial and non-financial information on operational and strategic levels; controlling the internal business processes; achieving, measuring and analyzing organizational performances. Modern cost systems like activity based costing (ABC) or target costing (TC), new managerial approaches like just-in-time, cost management systems, methods and management tools like balanced scorecard, benchmarking or customer relationship management become interesting and new topics among researchers.

The concepts and notions like "*administrative accounting*" or "*cost accounting*" used by researchers are replaced with the notion of "***managerial accounting***" equally highlighting the role of this activity in the decision making process.

**4.The management accountant's role – bean counter or business partner?**

As we emphasized in the previous paragraphs, in the last few years managerial accounting suffered a re-evaluation in terms of developing new and advanced innovations, techniques, methods and systems. These changes generated changes in the roles of management accountants also.

In the last years there has been an intense discussion among researchers and academics on the new roles of management accountants; (Siegel&Sorensen, 1999; Garg et al, 2003; Yazdifar&Tsamenyi, 2005; Jarvenpaa, 2009); accountants' roles and professional image have been the subject of media attention, accounting profession discussion and researcher investigation, being seen as interrelated yet at times contradictory (Warren&Parker, 2009).

Traditionally, the accounting profession and the accountant as a professional have been stereotyped as ”bean counters”, as employees whose work is to produce financial information of little decision-relevance (Warren&Parker, 2009) or as "watchdogs" and "number crunchers" (Byrne&Pierce, 2007). Business performance evaluation; cost and financial control;

cost cutting; presenting and interpreting the management accounts; planning and managing budgets; interpreting operational information were viewed as important tasks for management accountants (Yazdifar&Tsameny, 2005). Some studies note that management accountants play an important part in organizational decision making processes (Caglio, 2003); others (Byrne&Pierce, 2007) consider that management accountants must be aware of business priorities and market trends and they must become more actively involved in business processes. Yazdifar&Tsameny (2005) consider that besides business performance evaluation, productivity improvement, managing IT systems, strategic planning and decision making, must become the vital tasks for management accountants.

We can see that the literature is contradictory and it doesn't provide a consistent and complete picture of today's management accountant's role.

Still, analyzing the existing literature, we consider that Yazdifar&Tsameny (2005) emphasizes the most the changing roles of management accountants through their study. The two researchers conducted a survey among one thousand, randomly selected, qualified members of the Chartered Institute of Management Accountants on three main issues: (1) management accounting practices, tasks and techniques both in the 1990s and in the new millennium; (2) factors driving changes in management accounting practices; and (3) the roles of management accountants, skills and perceptions both in the 1990s and in the new millennium.

The table below gathers the findings of Yazdifar&Tsameny (2005) regarding the roles, skills and perceptions of management accountants in the 1990s and in the new millennium.

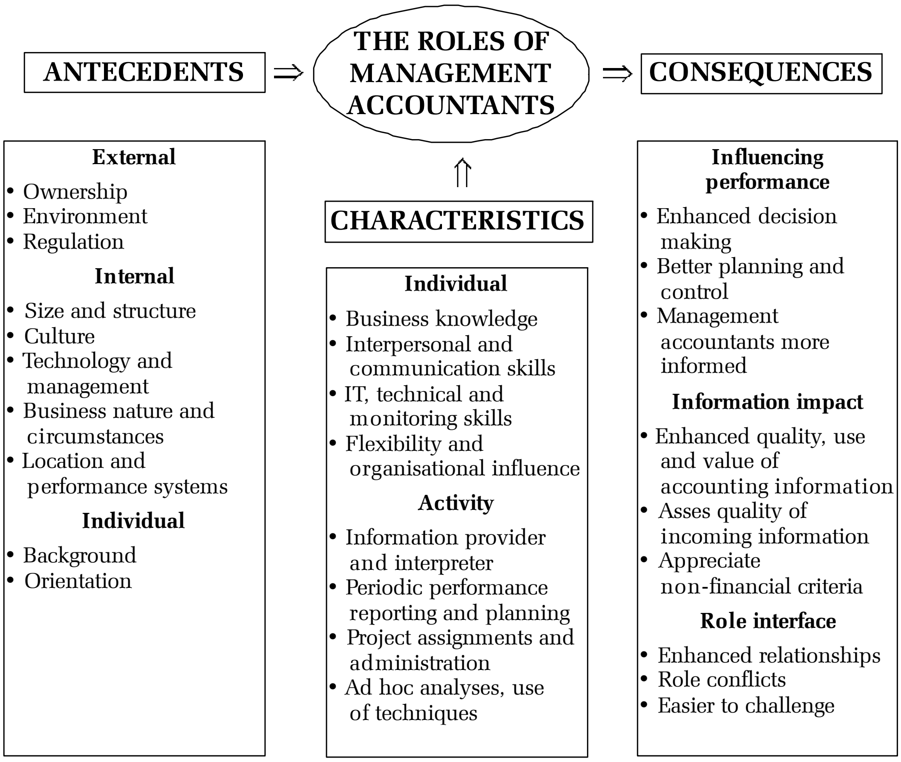
However, over the last years competitive environments and economic forces, management expectations, technological developments, the introduction of accounting innovations changed and moved the role of the management accountant from being oriented around number crunching and maintaining the overall functioning of the accounting system to an increasingly business-oriented role (Jarvenpaa, 2007). This idea is shared by other researchers also (Burns&Baldvinsdottir, 2005; Jarvenpaa, 2009; Birnberg, 2009). According to them the management accountants have to give up being "watchdogs" and they must become active advisors of management and increasing participants in decision-making being able to provide more added value to the management.

**Table 1. Management accountant's tasks and skills (past and future)**

| Management accountant's tasks and skills in the 90's | Management accountant's tasks and skills for the future |
|---|---|
| Business performance evaluation | Broad business knowledge, business performance evaluation |
| Cost/financial control;<br>Cost cutting | Cost calculation, cost analysis, cost management<br>Cost and financial control |
| Planning and managing budgets | Profit improvement; generation/ creation of value |
| Interpreting and presenting the management accounts | Strategic thinking and change management<br>Strategic planning and decision making |
| Interpreting operational information | Interpreting/presenting the management accounts |
| Implementing business strategies | Integrating financial and non-financial information; interpreting operational information |
| Profit improvement;<br>Capital expenditure evaluation and control | Working capital and short-term financial management |
| Implementing, designing new information systems | Become integrated into process-oriented managerial teams |
| | Increase work productivity and production processes |
| Team work<br>Oral communication | IT/ systems knowledge |
| Professional, ethical, interpersonal, commercial skills | Teamwork and leadership<br>Communication<br>Professional, ethical and interpersonal skills |
| Beancounters, scorekeepers, number crunchers | Business advocates, business analysts, business partners |

*Source: Yazdifar et Tsameny (2005)*

Indeed, we are witnessing the reposition of the managerial accounting profession in an increasingly global and technologically competitive environment in order to remain viable as a discrete and valuable profession (Warren&Parker, 2009). Considering these changes the figure below presents a comprehensive picture of the antecedents, characteristics and consequences associated with the roles of management accountants.




*Source: Byrne et Pierce (2007)*

**Figure 1. Antecedents, characteristics and consequences associated with the roles of management accountants**

In the end we can conclude that management accountants play an important role within organizations, in providing financial and non-financial information to all users, especially to managers; they have a direct contribution to the planning and control of organizational operations and a major impact upon organizational strategy and outcomes.

**5. Managerial accounting and the management accountant's role within Romanian organizations**

Managerial accounting has historical antecedents that stretch back to the beginning of the 1900s. Whether it was called *industrial accounting*, or *cost accounting*, or *administrative accounting* it is certain that concerns regarding expenses' classification and analysis, production cost calculation, pre and post cost calculations, resource consumption administration have existed since the beginning of the 90s. As a result, managerial accounting in Romania has had a certain evolution, a little different and slower compared to the international evolution, as it has been strongly influenced by political and social regimes and the development of Romanian economy (Volkán, 2010).

In 2002 Parker considered that managerial accounting is labouring under the shadow of financial reporting, auditing and taxation, it often casts in the role of „poor cousin" and it has been invariably relegated to a role of organizational cost keeping and budgeting and the obligatory but unremittingly dull university or professional body course on the delights of process costing and budgetary variance analysis. These ideas and beliefs were adopted by Albu (2006) who considered that in Romania financial accounting and reporting has dominated the accounting area to the detriment of managerial accounting and this results that firms have inadequate information for cost management, organizational performance planning, monitoring and control. Fiscal dominance, taxation, reduced understanding of the accounting information utility by managers, resistance to innovation, lack of collaboration between managers and accountants were just a few factors impeding the development of managerial accounting.

Consequently, these aspects and factors had a great impact on the accounting profession also. Within Romanian organizations Albu (2006) found significant variations referring to the title, duties, required skills and competences of those who are involved/working in the field of managerial accounting. Albu (2006) identified 8 job-roles with different duties, responsibilities and skills: junior controller, financial manager, accountant for managers, controller, responsible for reporting, management accountant, controller and financial analyst. The table below shows the competences and responsibilities required from Romanian professionals.

**Table 2. Skills and competences of Romanian professionals in the field of managerial accounting**

| Job-role | Required skills and competences | | | | |
|---|---|---|---|---|---|
| | **Intellectual** | **Technical** | **Personal** | **Interpersonal** | **Organizational** |
| 1. Junior controller | Logical thinking<br>Creativity | Planning<br>Performance analysis | Good time management<br>Timeliness | Communication | Understanding of commercial activity |
| 2. Financial manager | Strategic thinking | Accounting<br>Financial planning<br>Reporting<br>IT | Managerial attitude<br>Ambition and motivation<br>Integrity, ethics and maturity | Communication<br>Team working and coordination | Human resource management<br>Project management<br>Organizing and delegating tasks |
| 3. Accountant for managers | Attention to details | Accounting and finance | Resistant to stress<br>Assign priorities and meet deadlines | Communication<br>Leadership | Support the decision making process |
| 4. Controller | - | Accounting<br>Control | Assume responsibility<br>Autonomy | Communication<br>Leadership | Management<br>Understanding of the production and industrial environment |
| 5.Responsible with reporting | Proactive thinking | Accounting (IFRS, costs)<br>Control<br>Analysis and IT | Resistant to stress<br>Timeliness<br>Well organized | Team working | - |
| 6. Management accountant | - | IT (data bases, software)<br>Accounting | Timeliness | - | - |
| 7. Controller | - | Financial analysis<br>Reporting | Determination | Team spirit<br>Motivation<br>Communication | - |
| 8. Financial analyst | - | Accounting<br>Budgeting<br>Costing<br>IT | Dynamism<br>Motivation<br>Positive attitude<br>Resistant to stress | Leadership<br>Communication | - |

*Source: Albu (2006)*

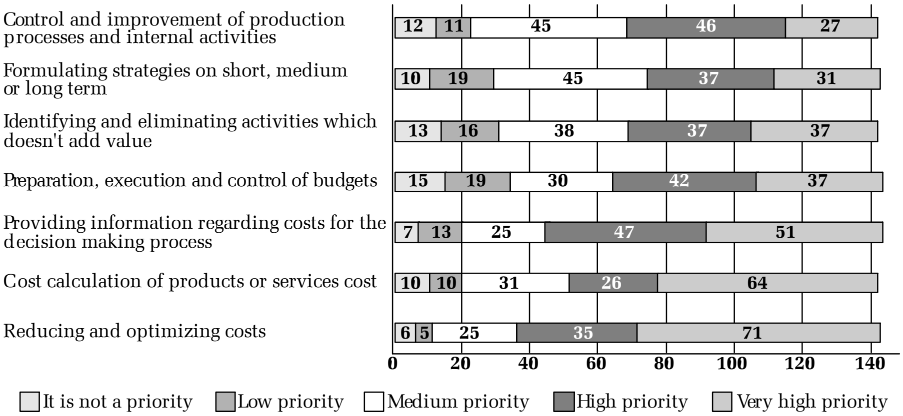
After a closer look at the table above we can conclude that Albu (2006) identified significant changes both in the definition and scope of managerial accounting, and the roles, powers, skills and competences of the professionals who work in this area. We can notice that there is a wide variety of positions and job roles within Romanian organizations, positions which require skills and responsibilities of different strains. This can be the indication of the degree of development of managerial accounting and managerial accounting practices in Romania. In some companies managerial accounting means budgeting, costing, analysis and reporting of production, diagnosis and reporting of financial statements; while other companies (only a few of them) consider that the role of managerial accounting is to be an advisor of the management and to support the decision making process. These companies realized that strategy implementation and performance planning and control, through appropriate tools and principles, could be the solution of continuous improvement. Moreover, there is an emphasis on personal and interpersonal skills of professionals working in the field of managerial accounting. Communication, team working, flexibility, motivation, leadership are just a few requirements of today's professionals.

Four years after Albu's study and analysis, after analyzing the current stage of research we found out that academics and researchers seem to recognize the importance and necessity of managerial accounting and cost calculation. Wishing to know if the same enthusiasm is shared by practitioners, we (Volkan, 2010) developed a questionnaire on the organization and conduct of managerial accounting and cost calculation within Romanian companies, addressing it to professional accountants, members of The Body of Expert and Licensed Accountants of Romania (CECCAR).

With the questionnaire we tried to cover the following issues: (1) managerial accounting aspects of organizations: managerial accounting systems implementation, cost calculation methods and aspects, cost management within Romanian companies; (2) issues regarding the use and utility of managerial and cost accounting information in the decision making process. Our questionnaire was sent to a number of 1871 professional accountants, members of CECCAR, having a response rate of 9,52%.

After processing the data obtained we found that Romanian organizations seem to recognize the importance and necessity of managerial accounting and cost calculation, as they are implementing managerial accounting systems. However, in implementing managerial accounting, organizations do not rely on current regulations and the proposed scheme, rather preferring to develop their own methods and techniques.

Another confirmed aspect, presented in figure 2, is the Romanian organizations' focus on cost calculation; most of the questioned organizations associate managerial accounting with cost calculation. For 71 of the respondents *reducing and optimizing cost* is a main priority; for 64 respondents *cost calculation of products or services costs* represent a main priority; and 51 of the respondents considers that *the role of managerial accounting is to provide information for the decision making process*. On the other hand only a few of the respondents consider that managerial accounting helps companies to formulate and implement strategies; to control and improve production processes and internal activities; or to identify and eliminate redundant activities.

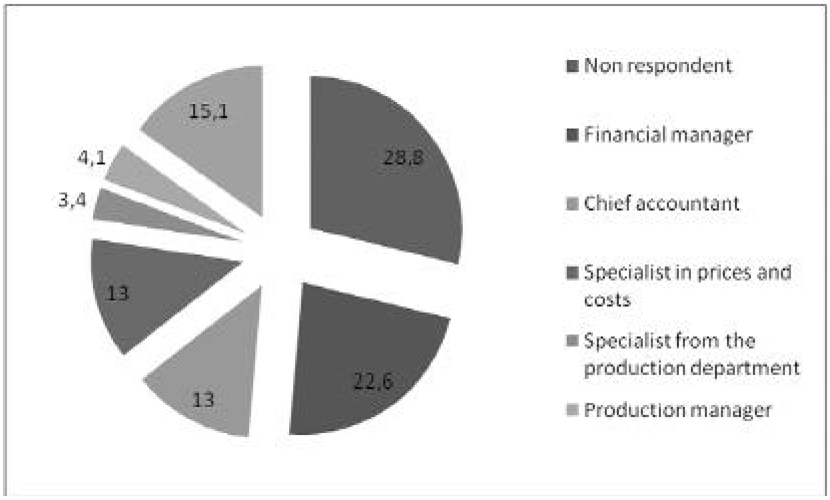



*Source: author's analysis based on the data collected*

**Figure 2. The role of managerial accounting within Romanian companies**

As we mentioned earlier in many Romanian organizations cost calculation and management seems to be the top priority. Cost type of information is used to determine the selling prices of products and services; to decide the purchase or production of certain products; to design and develop market and customer oriented products or services; to determine ways to improve products or production processes.

As for the professionals acting and working in the field of managerial accounting our study shows that the practice is still contradictory and it doesn't provide a consistent and complete picture of today's management accountant. The figure below shows that in Romanian companies managerial accounting and cost management activities are fulfilled by financial or production managers, chief accountants, specialists form the production departments or by other persons like the general manager, the controllers (controlling department) or the administrator. We found out that in small companies the general manager or the accountant is the person with managerial and cost accounting preoccupations also, while in medium sized and big companies specialists from the production departments or production managers, chief accountants, controllers or controlling departments fulfill the job of management accountants.




*Source: author's analysis based on the data collected*

**Figure 3. Professionals associated with managerial accounting and cost management**

The main conclusion of our study is that within Romanian companies the concept of management accountant is very rare. Romanian companies have accounting departments, financial managers, chief accountants, financial accountants or specialists in cost calculation. Often, the accounting professionals are overloaded with financial accounting and reporting activities; they seem to be more preoccupied with the preparation and timely filling of the statements and reports required by the government agencies. Under these conditions managerial accounting and the management accountant can't become active advisors of management and increasing participants in the decision making process.

Moreover, the results of our research undertaken in 2010 did not differ greatly from the conclusions formulated in 2006 by Albu, according to which in Romania we can find significant variations in the title, duties and responsibilities of the accounting professionals.

**6. Conclusion**

With our study we wanted to find out how managerial accounting and managerial accounting profession evolved in the last years. Firstly, we were interested on the opinions of researchers from international level. The main conclusion is that, on international level, managerial accounting evolved considerably, became an active advisor of management because only based on the information supplied by managerial accounting, managers can plan, analyze and control internal activities and processes; they can also establish long, medium or short term strategies; they have the possibility to manage resources efficiently and they can eliminate those activities that do not add value to the organization.

Secondly, we wanted to identify the way managerial accounting and the managerial accounting profession is perceived by Romanian researchers, academics and practitioners. The main conclusion is that in Romania managerial accounting had a different and slower evolution compared to the international evolution, and it has been strongly influenced by political and social regimes and the development of Romanian economy.

In the last years we noticed an increased interest of Romanian researchers and academics towards the field of managerial accounting. Moreover, the positive international influence is felt in what concerns the guidelines of managerial accounting, cost calculation methods tools used in the decision making process and the organizational performance measurement process. It is these influences that make us feel more optimistic about the evolution of Romanian research in managerial accounting and cost calculation.

Regarding practice the main conclusion is that many Romanian organizations seem not to understand the importance of managerial accounting, neglecting in this way aspects related to the analysis of expenses, cost management or the implementation of procedures and methods to generate added value. Managerial accounting still faces gaps, it is still considered *"the poor relative of financial reporting, auditing and taxes"*, it is associated *"and forever tied to an organizational role of calculating costs and budgeting*" while managerial accounting is much more.

Romanian organizations need managerial accounting professionals "armed" with skills and expertise, adequate knowledge in the field of accounting, IT systems, management and marketing, personal and interpersonal skills, who are willing to learn production and internal process technologies. They need professionals willing to work in interdisciplinary teams, being at the same time advisers and management consultants not only in the decision-making process, but in the everyday work of organizations.

This "reform" should continue with more stringent regulations; interest from management; concern and commitment from managerial accounting professionals and cooperation and effective communication to / between all hierarchical levels within organizations, respectively. Only this creates a strong managerial accounting system which can become, at the same time, advisor for the management in the decision making process.

Moreover, we consider that globalization fosters fierce competition and the growing momentum of organizations will be felt among Romanian organizations, which will lead to the development of an interdisciplinary managerial accounting, flexible and adapted to the needs of each business, using their own tools for processing, presenting and making use of information. These changes bring a "ray of hope" because they reinforce the belief that new methods of calculation and management systems will become the centre of attention, not only of researchers but also of practitioners and organizations. Value and performance will gradually become two concepts that will characterize any modern management of Romanian organizations.

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# Implementing Enterprise Resource Planning, the Case of Small and Medium-Sized Enterprises in Romania

GYÖNGYVÉR KOVÁCS[1] – MIHAI AVORNICULUI[2]

**Abstract**

In our days, corporations often must operate in a constantly changing environment, while they must perform the necessary tasks of their key processes. ERP gives more visibility on data across the entire corporation, speeds up communications facilitating the exchange of data across corporate divisions.

When a small or medium-sized enterprise can exploit the benefits from using an ERP system, it significantly enhances the performance of the organisation's business operations.

In this paper we examine the situation of ERP systems in Romania, as well as the challenges of implementing ERP systems for small and medium-sized enterprises.

**Keywords**: ERP Systems, SMEs, system implementation, integrated solution

**JEL Classification:** M15

## 1. Introduction

In our days, more and more people can hear about the potential and importance of ERP systems. However, implementing a new ERP system does not always guarantee successful results. ERP implementation can be a considerable drain upon an organization in terms of both cost and development time, and the result does not live up to expectations.

The predecessors of the ERP systems are considered the MRP (Material Resource Planning) systems. They tried to answer the question of how much material is needed for a production process. Material Requirements Planning simulates the universal manufacturing equation. It uses the master schedule (What are we going to make?), the bill of material (What does it take to make it?), and inventory records (What do we have?) to determine future requirements (What do we have to get?) (Wallace & Kremzar 2006).

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In the 1970s, the so-called Closed Loop MRP systems were created, which contain tools to address both priority and capacity, and to support both planning and execution. By 1980, it became necessary to integrate the manufacturing process with additional resources, so the next step in the evolution is Manufacturing Resource Planning or MRP II. Ideally, it addresses operational planning in units, financial planning in dollars, and has a simulation capability to answer "what-if" questions. Manufacturing resource planning is a direct outgrowth and extension of closed-loop MRP.

Additionally, systems such as CAD (Computer Aided Design), CAM (Computer Aided Manufacturing), CAL (Computer Aided Learning) tried to make up for the shortcomings of MRP II.

In the 1990s, appeared the fully integrated solution, the ERP. The following section will explain this system.

For a graphical view of the evolution of ERP systems, see Figure 1.

**2. Definition of ERP**

The use of concept ERP as an integrated enterprise resource planning information system (a software) or enterprise resource planning as an enterprise-wide set of management tools is still not completely clarified.

Wallace and Kremzar defined ERP as follows: ”ENTERPRISE RESOURCE PLANNING (ERP) predicts and balances demand and supply. It is an enterprise-wide set of forecasting, planning, and scheduling tools, which:

• links customers and suppliers into a complete supply chain,

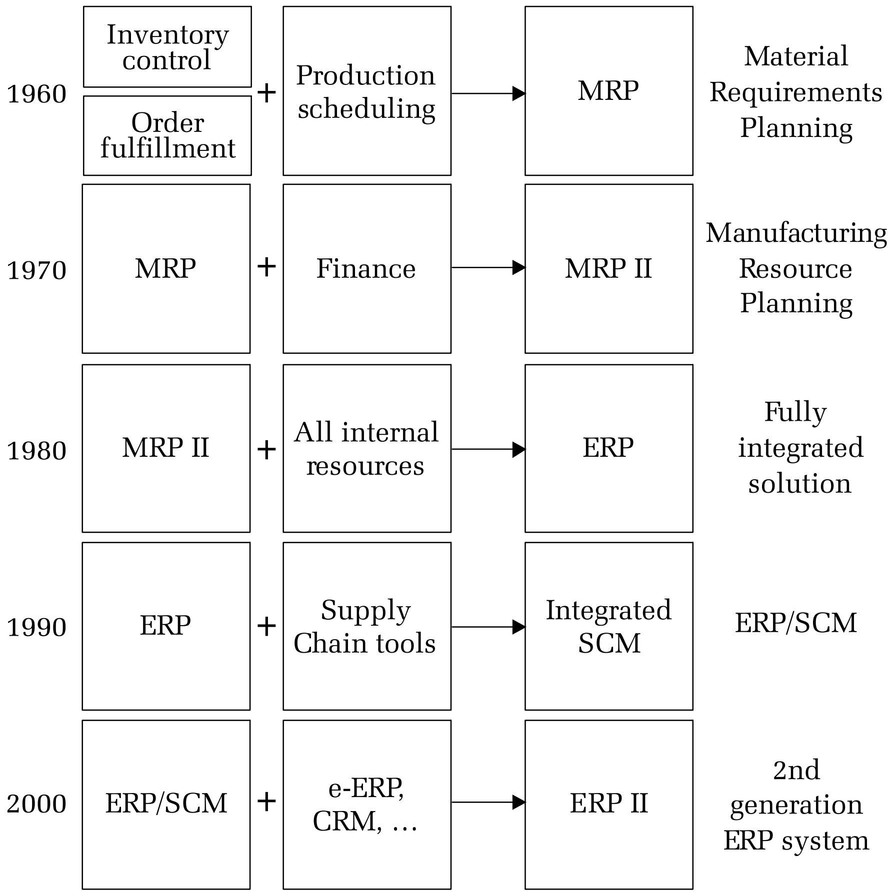
• employs proven processes for decision-making, and

• coordinates sales, marketing, operations, logistics, purchasing, finance, product development, and human resources. " (Wallace & Kremzar 2006)

ERP systems are also being referred to as “enterprise systems” (ES). However, other authors use this acronym to refer to software. In his book Mission Critical, author Thomas H. Davenport describes enterprise systems as ”packages of computer applications that support many, even most, aspects of a company's information needs.”

The functionality of an ERP system covers the following:

• Production planning
• Sales management




*Source: Turban, McLean, Wetherbe 2002*

**Figure 1. The evolution of ERP**

- Inventory control
- Effective supply chain management
- Customer service
- Order Tracking
- Financial records
- Human Resource Management
- E-commerce

In the past 10 years, ERP vendors have increased their product offerings to target and work with midsized companies to capture this huge market opportunity.

### 3. Advantages and disadvantages of ERP systems

It is important to mention the benefits and costs of ERP systems, as they affect the introduction of these systems.

The benefits of ERP systems can be summarized as follows:

- direct access to a wealth of information: the system can quickly respond to user requests;
- increased quality of information provided to enterprises: since the system possesses a unique database, should always be able to deliver quality information;
- applicability: the system is easily reconfigurable in case of economic changes;
- optimal data storage and operations: the system's database storing and rationalizing redundant data;
- the system is well maintained: the system can be modified by a specific company, if necessary;
- collaborative dimension: CRM and SCM modules can be added to the system;
- opening in the direction of e-business: the ERP system architecture allows the integration of e-business applications;
- cost reducing: a well-designed system leads to decreases in lead times, purchase costs;
- effective planning of all the company's resources: a good ERP system can cover the complete resource planning;
- overall improvement in productivity: an ERP system improves productivity;
- profit maximization: in case when the system adapts to the market expectations.

As disadvantages of the ERP systems, we can mention the following:

- complexity: it's not easy to design and implement an ERP system;
- high costs: the implementation of an ERP system is expensive;
- the time requirements are very large: as the system is generally complex, it takes a lot of time to implement;

• dependence on the supplier: it may be that there is only one supplier and the company depends on it;

• not appropriate use of the modules: it can happen that the enterprise may not choose the right system for his needs.

In summary, although implementing an ERP system may be costly and time consuming, the benefits are worthwhile.

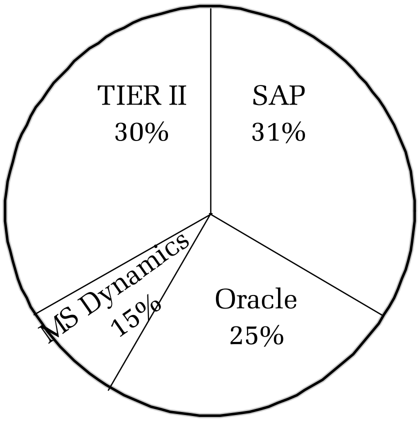
**4. ERP systems in the world market**

Despite the economic crisis, business applications, including ERP systems began a slow recovery in the world market.

ERP software market increased to 24.5 billion $ at the beginning of 2010, compared to 23.8 billion in 2009.

Historically, the dominant vendors on the ERP systems market were only three, namely SAP, Oracle and Microsoft.

Figure 2 indicates market share by major vendors in 2009. Of course, this distribution varies depending on what sized businesses the respective ERP system is addressed to.




*Source: Panorama Consulting Group, 2010*

**Figure 2. Major Vendors' Market Share in 2009**

One point of note is that Tier II vendors have increased their market share from 23% in 2008 to 30% in 2009.

Epicor, Baan, Sage, Infor, IFS, QAD are considered Tier II solutions.

Also, there has been a lot of growth in the last ten years on web based enterprise applications such as SaaS applications, or software as a service, that have change the ERP market share profile.

The ERP industry has dramatically innovated with new web based products such as software on demand applications or SaaS, software as a service solutions that have been skyrocketing in demand from companies of every size and capturing significant market share from on-premise ERP vendors with robust solutions that are easy to use, easy to deploy, and significantly more affordable.

For smaller businesses, it gives the user the opportunity to finally enjoy the benefits that an ERP solution can deliver to an organization by eliminating the major capital requirement hurdle.

**5. ERP systems, the situation in Romania**

At the end of the year 2008, the strengthening economic crisis had a major influence at companies looking for an ERP solution, because they are targeted toward lower-cost products.

A current report by global market research and strategic consulting firm Pierre Audoin Consultants (PAC) assesses that the ERP market in Romania dropped by 17% in 2009, compared to year 2008. For 2010, a decrease of 4% will be expected.

Growth in the ERP market in Romania only in 2011 is expected. The return to an above 20% annual growth rate is not expected before 2012, in the context of multiplying public projects and of a more optimistic attitude in the trade area, especially that of medium-sized and large companies.

According to PAC study results, S&T Romania continues to be the leading ERP system integrator in Romania, with a market share around 23% in 2009, followed by IBM and NESS, despite the fact that their income is reduced in the recent period.

If we consider the total ERP market in Romania, TotalSoft is located in the top, based on revenues, followed by Oracle and SAP.

According to PAC data, the value of the ERP market was 120, 6 million euro at the end of year 2008. By the end of the 2009 this figure has gone under 100 million euro. In 2008 the CRM (Client Relationship Management) segment was 7.8 million Eur, compared with 6.6 million Eur in 2009. The BI (Business Intelligence) applications market value was 10.7 million Eur in 2008, while in 2009 increased to 11.7 million Eur.

The BI and CRM has small and fragmented market in Romania. At the top, there are only a few companies, the rest is very spread.

The economic crisis has a great impact on the CRM market and a visible reduction will be observed. The BI segment is less affected by the crisis, but it will not be experiencing too much growth.

In the last few years ERP vendors and enterprise software developers are trying to cover a larger range of businesses with their systems. One such developer is Epicor, which provides solutions to SME sector. In 2010 the company releases Epicor 9 in Romania, introducing a new approach to the way enterprise resource planning (ERP) systems and business software solutions are designed, built, and used.

Another competitor in the SME market is Microsoft. They are not leaders of this segment in Romania, but offer good solutions for SMEs. The compatibility with the Microsoft Office products, which has a wide user base, is also a key component of their popularity.

Another company, BIT Software from Brasov implemented solutions that can be used successfully by enterprises with 50-250 employees. They implemented ERP & CRM-type system, the first "open source" system in Romania. Their system, called SocrateOpen, was implemented on Compiere platform.

In the current circumstances, the success of ERP packages implemented for SME also depends on how they can integrate systems such as CRM, SCM, BI and Internet-specific applications.

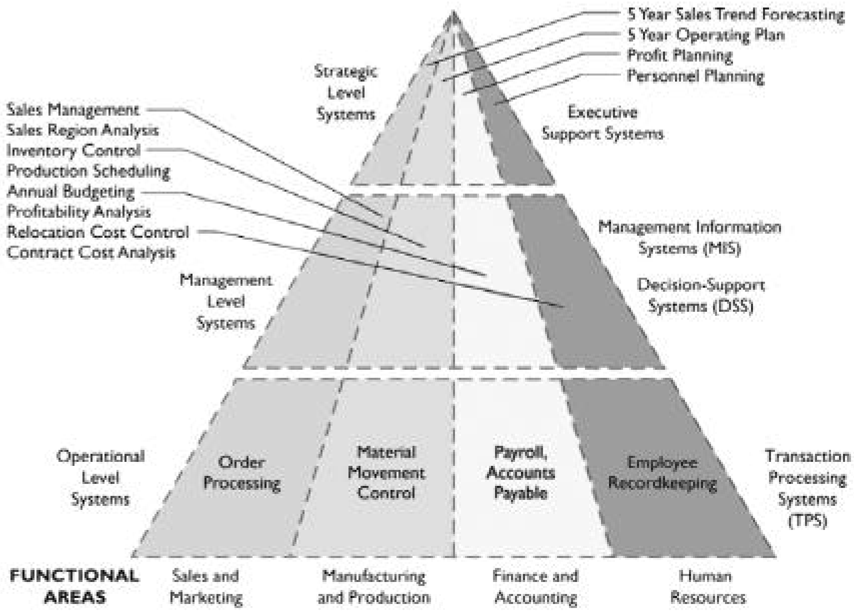
The development of integrated systems is also affected by new e-commerce and e-business opportunities, which have to be integrated in the ERP systems in the near future. Given the economic uncertainty of the past years, PAC predicts that in 2011 only slow growth on the ERP systems market can be expected.

For the 2010–2014 period, the average annual growth of the ERP systems market in Romania is expected to be around 14%. This growth will be perceptible also in the SME market.

**6. The challenges of implementing ERP systems**

ERP implementation is a social-technical challenge. The primary purpose of implementing ERP is to improve the corporate governance process. This does not mean process automation, but making them more efficient.

Each business function has its own specialized information system at each level. This can be seen in Figure 3.




*Source: Laudon & Laudon, 2006*

**Figure 3. Information pyramid**

An ERP system development permeates the whole enterprise, changing the expectations, processes, and is important to manage them properly. When considering the decision to invest in an ERP system, a business case must be developed to provide an understanding of ERP and to formally assess the benefits that the company can expect to achieve. The analysis must consider not only the cost/benefits analysis, but also the non-financial factors. ERP implementation can be disastrous for companies that fail to manage the implementation process.

The ERP system development can only be effective if it takes into account the specificities of the enterprise and adapts to them, but also influences the processes, the organization and structure.

In a company's lifetime, implementing an ERP system is usually a one-time task. Therefore, efforts should be made that the process to happen more effectively. It is possible that the involvement of external experts may be needed, since not all businesses have the necessary personnel to achieve this task.

Many companies today need to re-implement. Some of these are companies who thought they were implementing ERP, but actually were only installing enterprise software (Wallace & Kremzar 2006).

There are many strategies for implementing ERP. The most widely discussed ERP implementation strategies are (Avdejenkov et. al. 2009, Laudon & Laudon, 2006):

• *Big Bang*: Implementation happens in a single, major event. All modules are installed across the entire organization, users move to the new system on a given date.

• *Phased rollout*: Changeover occurs in phases over an extended period of time.

• *Parallel adoption*: Both the legacy and new ERP system run at the same time. Users learn the new system while working on the old.

• *Slam-dunk*: In this method the focus is on just a few key processes, such as those contained in an ERP system's financials module. The goal here is to get ERP up and running quickly. The slam-dunk is generally for smaller companies expecting to grow into ERP.

Of course there is no one-fits-all solution when it comes to implementing an ERP.

Risk factors most likely to occur during implementation, based on the literature reviewed (Willcocks et. al. 2003, Summer 2003, Holland & Light 2003):

• lack of motivation: not precisely defined what is expected from whom and how to reward;

• disorganization: the project team is not suitable;

• lack of feature-function fit between available packages and company needs: they want the system to adapt the existing processes;

• users do not understand the basic concept of the system: employees need training in order to use it to continue day-to-day operations and to understand how the system will change business processes;

• not adequately assessed IT needs: you may need to modify the system;

• the financial plan is impractical: most implementations go over budget (over 51%);

• bad corporate communication of the project: the employees do not have enough information on the project;

• There are no clear metrics: we do not know exactly what to expect from the system in short- and long-term;

• Lack of top management commitment: the management imagine only an IT project;

• the functions of the system are not clearly defined: the functions will not be suitable for management;

• data conversion problems: transferring data from the old system may not be successful;

• the developer and the client can not understand each other: the professional language-speaking individuals cannot reach a consensus;

• the system facing technical challenges: there may be compatibility problems.

Consequently, the implementation of ERP systems for small and medium businesses is prominently a managerial activity. Managers must know and understand the implications of the system. They must be aware of changes that will take place and must agree that the change is necessary and possible.

Another important issue in the case of small and medium-sized enterprises is to purchase or to develop an ERP software system. Selecting a system is not easy, because they are difficult to acquaint.

Due to complexities of implementing an ERP system, most companies choose to hire a consultant to help select, configure and implement the system. This approach has the drawback that the consultant firm does not have adequate insight into the processes of the company. Also, the cost of hiring consultants can be very high.

Since every company has its own specific processes, each individual case requires a unique decision to develop a system or to select and implement an existing system.

In the reviewed literature, many studies try to give advice on how to select a system, however the financial approach is usually disproportionately pronounced (Avdejenkov et. al. 2009, Forslund 2009, Ifinedo & Nahar 2007).

There are more cost estimation models available, such as COCOMO (Constructive Cost Model), and COCOMO II.

TCO (Total Cost of Ownership) analysis was popularized by the Gartner Group in 1987. Today, TCO analysis is used to support acquisition and planning decisions for a wide range of assets that bring significant maintenance or operating costs across a long usable life. This will help to complete the IT project evaluation.

The major problem of IT developments of Romanian small and medium-sized enterprises is lack of resources. These enterprises are not engaged in investment calculations.

The SME sector has simpler hardware and software systems, and also the IT skills are scarcer. This sector predominantly using existing products, the individual development is rare.

The implementations and the resulting experience are growing rapidly.

**7. Conclusions**

ERP is widely acknowledged as having the potential to radically change existing businesses. ERP provides real-time integration of sales, operating and financial data.

The company must be prepared to use a comprehensive ERP system. This assumes that in the enterprise the responsibilities and tasks are well-defined. The implementation of ERP can be classified in the long-term decisions, therefore, above all, through-out strategy should be developed.

As it was shown, the implementation of ERP is not only a technical task, installing enterprise software, but also hard management work in order to improve business processes. ERP packages force an organization to implement a proven set of business processes. Therefore top managerial support is very important.

In the past few years, ERP vendors and enterprise software developers are trying to cover a larger range of businesses with their systems. For smaller companies in particular, SaaS based system should be considered as a real viable enterprise application option.

When used properly, ERP systems can help SMEs to optimize their business processes, to bring improvements in efficiency and effectiveness and ultimately to obtain competitive advantage.

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# Guide for Authors

The Economists' Forum invites papers presenting the conclusions of theoretical or applied economic studies, scientific debates, or book reviews.The articles can be written in Hungarian or English (for the special issue). The articles should be submitted to one of the following e-mail addresses:

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The text should be between 15 and 20 printed pages, numbered, A4 format, characters Times New Roman 12, single spacing.

The first must contain the title of the article, the author's name, their complete scientific title and affiliation (professional address, phone, e-mail), followed an abstract of 5–10 lines, that should present the main results of the article. The abstract will be followed by 5-7 keywords.

The authors are also required to submit an English and Romanian abstract with keywords in a separate document.

The presentation of bibliographical references:

In the text the references quotes will appear between brackets, with the name and the publication date, e.g.: (Gyeroffy 1997). For two co-authors they will use for example (Black and Scholes, 1973). In the case of three or more than three authors, only the first will be mentioned, under the form (Barberis et al., 1998).

If two references have the same author and the same publication year, they will be differentiated through letters (Fama, 1965a). These letters will also appear in the bibliography.

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Books: The list of authors including the first name initial and the year of publication, the title of the book in italics without abbreviations, the publishing house, the place of publication.

# Abstracts

## Banking Sectors in South-Eastern European Economies

**YIWEI FANG – IFTEKHAR HASSAN – KATHERIN MARTON**

It has been a major achievement that within a decade subsequent to military conflicts, embargo, and crises in the Western Balkan region, a privately owned banking sector developed in SEE that provides financial services similar to those of Western Europe. Rapid privatization ended government interference in the banks and foreign ownership contributed to the build-up of trust of the population that was fractured in several countries through actions of the central bank and other authorities.

The global economic crisis exposed some of the strength and vulnerabilities of SEE countries where mostly during the last decade banking sectors moved from state- and collective ownership to predominantly foreign ownership. Since this is a relatively new phenomenon, government policy makers need to adopt regulations that increase the benefits that foreign banks contribute to the local economy but also reduce some of the adverse impacts that are associated with foreign bank ownership.

**Keywords:** South-Eastern Europe, banking sector, financial intermediation, foreign banks

**JEL Classification**: G20, 21

## Framing Rural Employment Policy in the European Union in the Context of Sustainable Regional Development

**ANDREW F. FIELDSEND**

Many respected academics have questioned the appropriateness of the continuing close link between the Common Agricultural Policy and its 'rural development' measures. The European Union (EU) Framework 7 research project 'RuralJobs' included case study research on current employment patterns and opportunities for, and constraints on, rural economic diversification in five contrasting NUTS2 regions across the EU. As a contribution to the current debate on the shape of EU rural and regional development strategies for

the period 2014-2020, this paper presents the results of this analysis. Rural areas differ in their accessibility to urban centres with a population of 50,000 or more, but smaller population centres can be important employment and service centres for their rural hinterlands. An urban-focused approach to regional development could precipitate a 'race to the bottom' by excessively targeting funding at urban centres and contributing to the economic and social decline of the rural hinterlands. To comply with the priorities of the EU's Europe 2020 strategy, namely smart, sustainable and inclusive growth, regional development strategies should include a distinct rural component which recognises the potential contribution of natural capital, and therefore rural areas, to achieving a competitive regional knowledge economy.

**Keywords:** rural employment, European Union, regional development, accessibility

**JEL classification:** O18, Q01, R12

**Romanian Enterpreneurship in International View**

**ÁGNES NAGY – ISTVÁN PETE – ANNAMÁRIA BENYOVSZKI – LEHEL-ZOLTÁN GYÖRFY – TÜNDE PETRA PETRU**

The aim of this article is to identify Romania's place among the 71 countries, which participated in the Global Entrepreneurship Monitor project in at least one year between 2002-2009 time period, by entrepreneurship and economic development level. The study is based on individual and institutional variables, which are the main components of the Global Entrepreneurship and Development Index.

**Keywords:** Global Entrepreneurship and Development Index, entrepreneurial aspirations, entrepreneurial activity, entrepreneurial attitudes, Global Entrepreneurship Monitor.

**JEL Classification:** L26, O10, O57

**The Changing Role of Managerial Accounting and the Managerial Accounting Profession in Romania**

**ILDIKÓ RÉKA CARDOŞ – ISTVÁN PETE – VASILE DANIEL CARDOŞ**

In this article we discuss about the changing roles of managerial accounting and the managerial accounting profession. After analyzing the

existing literature in the field we would like to identify (1) how the objectives and functions of managerial accounting changed over the last years; (2) a set of characteristics, skills and competences of yesterday's and today's management accountant. We would like to point out that through accounting professionals managerial accounting becomes a business partner or analyst for every organization. After the international review the next step of our research is to identify the way managerial accounting and the managerial accounting profession is perceived by Romanian researchers, academics and practitioners. Our research results are based on previous studies made by Romanian researchers and a questionnaire based survey made by us among accounting professionals in Romania.

**Keywords:** Managerial accounting, management accountant, accounting profession, skills, competences, Romania

**JEL Classification:** M4, M10, M49

**Implementing Enterprise Resource Planning, the Case of Small and Medium-Sized Enterprises in Romania**

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In our days, corporations often must operate in a constantly changing environment, while they must perform the necessary tasks of their key processes. ERP gives more visibility on data across the entire corporation, speeds up communications facilitating the exchange of data across corporate divisions.

When a small or medium-sized enterprise can exploit the benefits from using an ERP system, it significantly enhances the performance of the organisation's business operations.

In this paper we examine the situation of ERP systems in Romania, as well as the challenges of implementing ERP systems for small and medium-sized enterprises.

**Keywords:** ERP Systems, SMEs, system implementation, integrated solution

**JEL Classification:** M15