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## **BUSINESS CONSULTING AND CONSULTANTS ACCORDING TO ENTREPRENEURS**

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### *Summary*

*The Institute of Business Sciences of the University of Miskolc has made a survey among business consultants firms and enterprises using consultations, enterprises not using consultations, but planning to do so and those not using and not planning to use any consultations. In the survey 362 enterprises from B-A-Z county and 83 consulting firms participated chosen by representative sampling. [1] [2] [3]*

*In this paper we demonstrate how the effectiveness of the consulting service is evaluated by the entrepreneurs in B-A-Z county and the main characteristics of business consultants.*

The Institute of Business Sciences of the University of Miskolc contacted 600 companies in Borsod-Abaúj-Zemplén county in 2001 and we were able to have 362 queries (60%) filled out. The sample is representative by main profile of the company and location. [1] The rate of answer was higher among larger companies than smaller one, so larger companies are over represented. *Figure 1.* shows distribution of examined companies by staff:

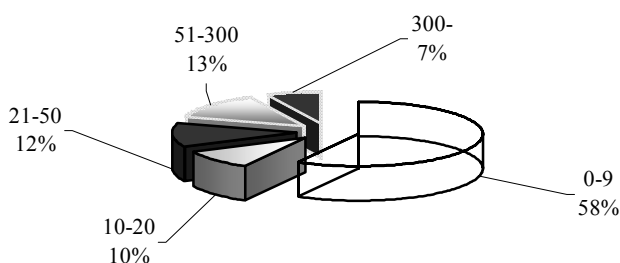


Figure 1. Distribution of examined companies by staff

Larger companies can better afford hiring consulting companies than smaller one –the rate of larger companies is higher among enterprises using consultations (115) than among examined companies (362): 36% are micro-enterprises (0-9 staff), 26% small-enterprises (10-50 staff), 21% medium-size enterprises (51-300), 17% big companies.

### Experiences of business consulting service

Figure 2. shows the evaluation of business consulting service according to the experiences of entrepreneurs (115):

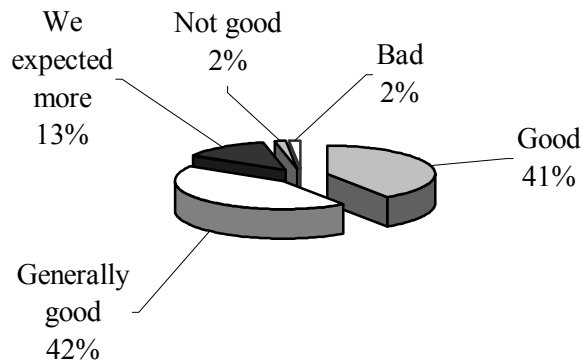


Figure 2. Experiences of business consulting service

Almost all entrepreneurs (83%) were satisfied with consultant, according to their experiences they would entrust him again. 41% were so satisfied, that they recommend others to entrust consultant. An insignificant part of the entrepreneurs (4%) were disappointed of consultant, according to bad experiences only 2% ruin the reputation of the whole consulting profession.

The companies marked the rate of the successful/unsuccessful and neutral projects. The results are similar to the former figure: they form their opinion about consulting service and consultant according to the efficiency of the projects. The rate of the successful projects is the dominant: 83%, the rate of the unsuccessful projects is only 9%.

### The effectiveness of service by consulting areas

Figure 3. shows the rate of the successful/unsuccessful projects by consulting areas:

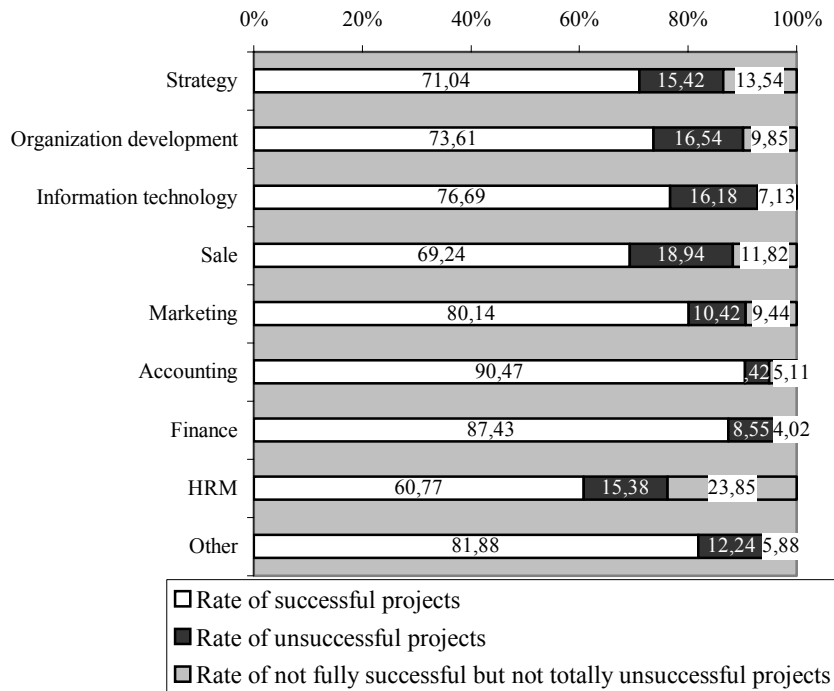


Figure 3. The effectiveness of service by consulting areas

According to our survey the rate of successful projects is dominant on each consulting area.

The most popular and efficient consulting areas are accounting and finance in our county. 52% of consulting projects focus on these areas. Experts easily solve problems in this field. They evaluate the financial situation of the company, do the bookkeeping, and prepare the tax returns on time, do tax advising. The frequent change of tax and law regulations increases the need of hiring an external expert.

Hoványi differentiate consulting areas according to successful consulting attitude: there are some consulting areas (e.g. Property valuation, auditing, information system organisation, logistics, production-organisation...) where consultants act in “professional role”, in other areas (e.g. HRM, strategy, reorganisation, corporate management, change management, marketing...) consultants act as “equal partner” or play second fiddle (they put client on the right track, but the solution occurs to the client). [4]

According to our survey clients evaluate consulting service more successful on those areas, where consultant acts in “professional role” (e.g. accounting and finance). Consultants are evaluated more critically on those

areas, where they act as “equal partner” or play second fiddle (e.g. HRM, sale, strategy, organisation development).

### The effectiveness of consulting firms by sizes

Figure 4. shows the effectiveness of consulting companies by sizes:

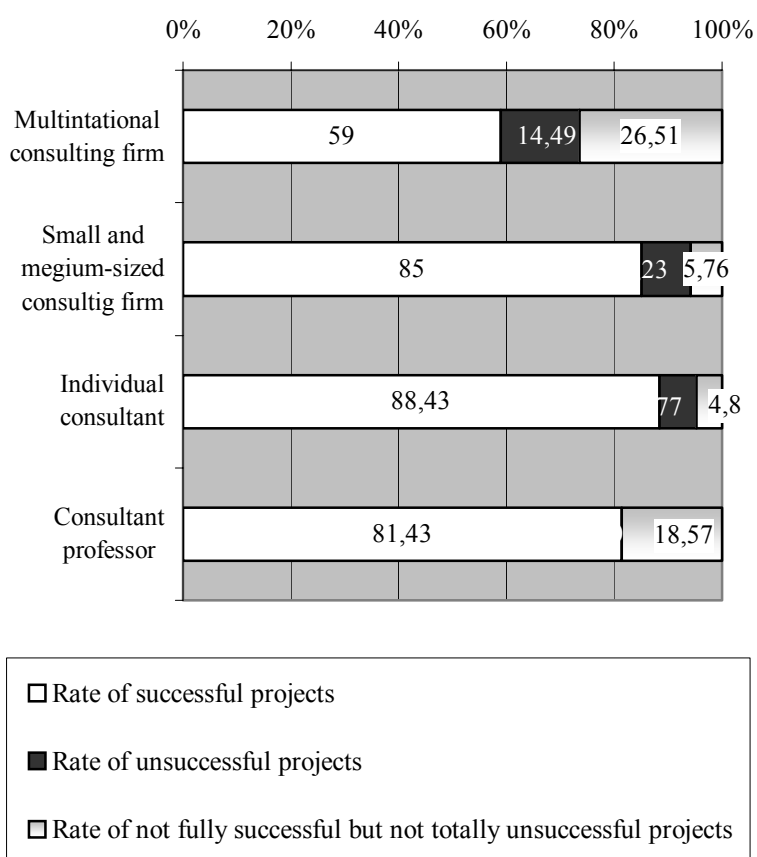


Figure 4. The effectiveness of consulting firms by sizes

Note: 12,4% of the entrusted consulting firms are multinational, 50,3% small and medium sized company, 34,5% individual consultant.

The majority, 85% of the B.A.Z. headquartered companies prefer **smaller business consulting companies** or **individual consultants**, 72% have entrusted firms from their own region (the North-eastern Region of Hungary). Almost all companies reported that the rate of the effective project is dominant. In case of consecutive less

effective projects the companies sought for another consulting company or got disappointed in the whole consulting profession. The companies in our county were more satisfied with the work of the small and medium-sized consulting companies in the region and the individual consultants. The local consultants have a better knowledge of the situation in the region, the local conditions and legislation. Their flexibility and knowledge of the local problems make them more convenient to the clients.

### Characteristics of consultants

We have analysed in both queries the most important characteristics of consultants. The entrepreneurs and consultants had to evaluate on a scale 1-5 the characteristics of consultants according to 21 criteria. "5" means: typical characteristic of a consultant; "1" means: absolutely uncharacteristic.

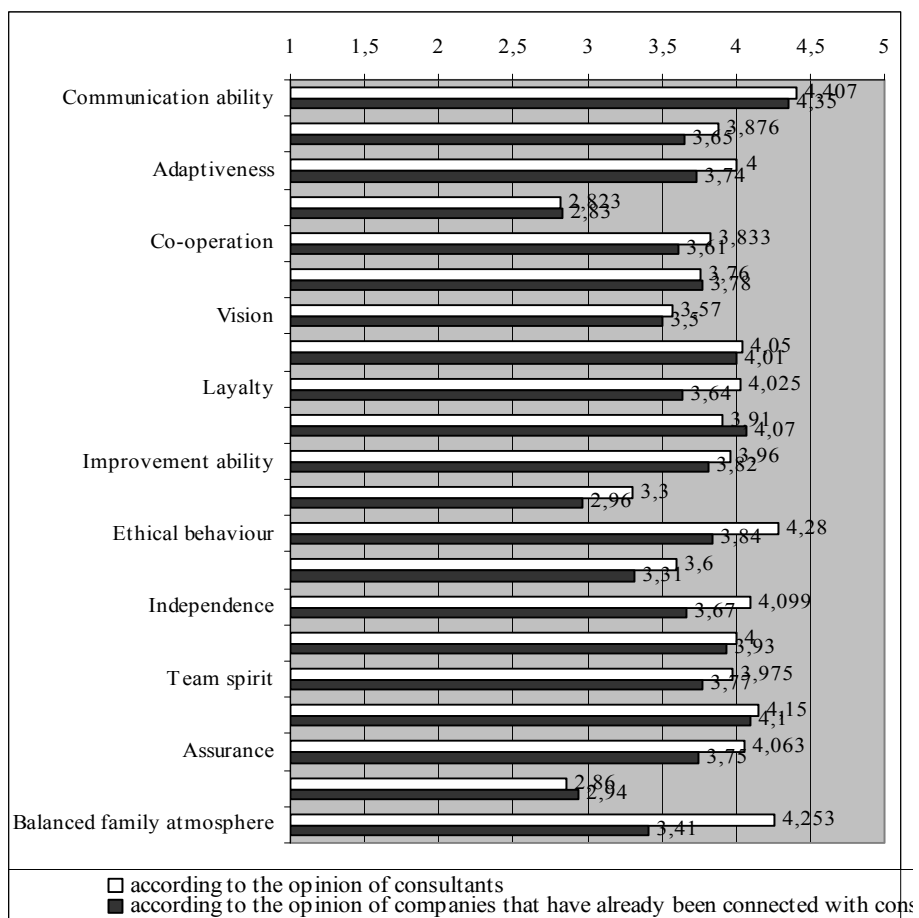


Figure 5. Characteristics of consultants

Both the companies and the consultants said the most important characteristic of the consultants is the **communication ability**. It is the characteristic needed to completely understand the need of the client, to get information, for a successful co-operation and for effectively answer the given questions.

Another important characteristic is **business spirit** – according to the subjects of the query the consultants are creative, able to develop and apply new alternatives.

The explosive development of **IT** played a major role in the consulting as well. Gained experiences and knowledge is not enough. Accurate knowledge of IT is needed to correspond to the client's needs. The consultants who aren't able to keep up with the newest IT trends will slowly disappear.

A must is **ethical behaviour** that balks abuse of the client's weakness or power. It is important for a consultant not to exceed its field of competence. The results showed that consulting firms believe this characteristic is a very important one (4.28 points). The clients think also it is important even though not that important – as shown in the result (3.84). It is interesting to observe that the companies that don't intend to make use of such a service are even more sceptical (3.34 points).

A **balanced family atmosphere** – as a characteristic – got 4.253 rating from the consulting firms. It plays an important role in developing effective co-operation conditions. The clients believe the consulting companies aren't really able to assure these conditions – and rated it at 3.41 points.

**Power based control** isn't characteristic among the consulting companies. Co-operation and team spirit is much more important – even though both parties believe it is only middle field characteristic.

An older **age** isn't specific for the consulting business. The belief that only an older aged person is capable of being a good consultant is obsolete. The actual belief is that also young people with less business experience but high education are capable of being good consultants.

**Ascetic behaviour** is not a characteristic of the consulting companies. Clients don't think that the consultants will deal with business problems keeping back family life or other programs – and they don't even expect them to do so.

## **Conclusion**

In this paper we demonstrated the judgement of business consulting service according to a survey conducted by the Institute of Business Sciences among business consultants and enterprises in 2001.

83% of the examined entrepreneurs were satisfied with consultant, according to their experiences they would entrust him again. The most popular and efficient consulting areas are accounting and finance in our



county. More than half part of consulting projects focus on these areas. The rate of successful projects on this area is 90%.

The majority, 85% of the B.A.Z. headquartered companies prefer smaller business consulting companies or individual consultants, 72% have entrusted firms from their own region (the North-eastern Region of Hungary). According to the survey the companies in our county were more satisfied with the work of the small and medium-sized consulting companies in the region and the individual consultants: their flexibility and knowledge of the local problems make them more convenient to the clients.

The most important characteristics of the consultants are the communication ability, business spirit and they are open to the information technology.

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## **KISS THE PRINCE AND FIND THE FROG**

Expectations and Reality About the Effectiveness of Multicultural Teams in Business Settings

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### **Introduction**

In the rapidly internationalizing world of business, no multinational company can escape from using multicultural work groups. Multicultural groups are most of the time mentioned as the great source for diverse thinking and therefore good basis for problem solving. However more and more studies have showed that opportunities that multicultural groups can provide have not necessarily taken all the time. Failures are just as common as success stories.

Why to use multicultural work groups then? The assumption of this paper is that there is a business pressure on multinational organizations to use such teams more and more.

### **1. Definition of Multicultural Teams**

Scholars have established different categorization for the levels of cultural diversity in groups. The following classification is based on the works of Adler (1992).

- Homogeneous Groups  
In homogeneous groups all members share the same cultural background. Therefore members of homogeneous groups generally perceive, interpret, and evaluate the world in a very similar way. Homogeneous can mean professional and national cultural background as well.
- Token Groups  
We talk about token groups when all but one member of a certain group share the same cultural background. Managing token groups can be a real challenge even if the leader of the team is the one culturally different member, which is often the case in business reality.
- Bicultural Groups  
By definition, in bicultural groups, two or more members represent each of two distinct cultures. This bicultural situation happens very often in case of mergers and acquisitions (M&A), when experts and managers from two companies try to integrate the cultures of the two merging organizations.
- Multicultural Groups  
In multicultural groups, three or more cultural background is represented on the ethnic level. It used to be large international organizations in the last

decade, where multicultural groups were in everyday use, but nowadays most multinational companies operate such task forces.

### 1.1 Definition Problems of Teams

Not even the word "team" has a common understanding in every culture. It differs from culture to culture. (Masnevski and Peterson, 1997) Three major perspectives are distinguished:

1. **Mastery Orientation**  
In for example Anglo-Saxon countries teams are considered as devices for decision-making. These „decision-making machines“ are operating by clearly defined goals, situations are always assessed, alternatives are generated and finally actions are taken. Mainstream management literature regards work-teams in this way.
2. **Relationships and Trust Orientation**  
In contrast to the previously mentioned approach and understanding, in Arab and Latin cultures, action is only taken after a level of trust in the relationship is achieved among the members of the team.
3. **Understanding Orientation**  
In Japan a team is formed to develop and reinforce understanding among members. Here trust is assumed by being the member of the group. Decisions are reached indirectly in interactions, which can hardly be called explicit to European norms.

## 2. Dimensions of Cultural Comparison in Team Work

In this section we would like to focus on the works of Kluckhohn and Strodtbeck (1952) and Hall (1990) bringing the dimensions of team related issues to focus. Therefore we considered only those measures which have a strong relevance for multicultural work-groups.

### 2.1 Kluckhohn's Six Basic Cultural Dimensions

<b>Orientations</b>	<b>Range of variations</b>
<i>What is the nature of people?</i>	Good(changeable/unchangeable) A mixture of good and evil Evil (changeable/unchangeable)
<i>What is the person's relationship to nature?</i>	Dominant In harmony with nature Subjugation
<i>What is the person's relationship to people?</i>	Lineal (hierarchical) Collateral (collectivist)

<i>What is the modality of human activity?</i>	Doing Being in becoming Being
<i>What is the temporal focus of human activity?</i>	Future Present Past
<i>What is the conception of space?</i>	Private Mixed Public

Table 1.: Kluckhohn and Strodtbeck's Six Basic Cultural Orientations

From the six dimensions of Kluckhohn (1951) we have found that all have a relevance on multicultural team work, albeit on a different level.

- The nature of people as a perception can influence the level of trust in teams from the beginning.
- People relation to nature (environment) is even more influential as a basic belief on what can be achieved and what cannot.
- Person's relation to people determines the acceptance and need for power in a group
- The modality of human activity strongly correlates with the inner need for keeping deadlines and schedules
- The temporal focus of human activity determines the planning process of the group and the understanding of the events surrounding the activities.
- The conception of space is more to do with the non-verbal side of communication in the team and the out-of-work activities.

## 2.2 Communication

As a starting point we can state that cultural communication is far more than the written and spoken messages. *"The essence of effective cross-cultural communication has more to do with releasing the right responses than with sending the "right" messages."* (Hall and Hall, 1990, p.4.)

In communication we can distinguish fast and slow messages. This characteristics are not really telling us about the speed of communication, rather the understanding time and duration of the messages. The problem is that very few people are aware of the fact that information can be sent by different speeds.

Almost everything in life can be grouped into fast or slow messages. Language itself is also a slow message. This even more applies to cultures, which can be only understandable for those who are taking their time and open their minds for such an experience.

People themselves are also slow messages as individuals. There is always a message in a person and definitely a slow one. But people with different cultural background are of course carrying a different message.

### 2.2.1 High Context and Low Context Cultures

By definition context is the event which surrounds an event, it is extremely connected to that moment and event. Hall distinguished the cultures of the world on a scale from low context to high context.

*"A high context communication or message is one in which most of the information is already in the person, while very little is in the coded, explicit, transmitted part of the message."* (Hall, 1976)

This difference influences every single aspects of life. Changing the context can have many meanings up and down the scale as well. For a high context culture, moving back down to a more formal low context means the message that something had gone wrong in the personal or working relationships. But this way of communication is only understood by people of that context, who are accustomed to use the silent language as well. Because low context people's approach to life is always segmented and based on discrete compartmentalized information, they always need detailed background information, before they begin to work somewhere or commit themselves to any project. In high context cultures people supposed to know a bit of everything what is going on around them. Therefore they can get very impatient and irritated by getting every piece of information from a low context person, who is assuming, the more information is told the better it is understood. On the other hand low context people can feel lack of information when a high context person is telling them about what (s)he thinks as important to know about the things. *"Too much information leads people to feel they are being talked down to; too little information can mystify them or make them feel left out."* (Hall&Hall, 1990, p.9)

### 2.3 Time

There are quite many dimensions to examine, when talking about time, but in business life two is extremely important. These ones are called *monochronic and polychronic time*.

*Monochronic time* means paying much attention on deadlines and commitments and also just doing one thing till it is finished. In contrast *polychronic time* means being involved with many things at once and not taking deadlines and commitments as carved in stone.

In monochronic cultures time is experienced and used in a linear way, it is divided into segments, scheduled and compartmentalized. Plans and schedules in monochronic cultures take priority above all and taken as sacred. In these cultures time is tangible, people talk about it as money, which can be *"spent"*, *"saved"*, *"wasted"* and *"lost"*.

Since monochronic system is built around doing one thing at a time, those who are ruled by it, do not like to be interrupted. This aspect has got many influences on relationships and business life. Some people are allowed to enter this limited time space, while others are not.

The world of business is highly infected by monochronic timing and is taken as natural.

*Polychronic time* in every aspect is the total contrast of the previously described one. Polychronic time involves many activities at one time and highly concentrated on relationship with other people. Human transactions are preferred to schedules. Conversations with friends and relatives, even on phone is rarely disrupted just to get to the next appointment on time.

Polychronic time is experienced less tangible than monochronic and more can be compared to a river than to a road. Understanding these differences of relation to time can be one's great advantage in international affairs.

### **3. The Organizational Level of Cultural Sensitivity**

According to Morosini (1998) the social environment in which the organization operates has a determinative influence on the methods-in-use. Therefore, beside the obvious internal and external factors, social embeddedness of the organization must be considered to thoroughly understand its market behavior and the role of cultural values in the process.

The organizations social components include such aspects as:

- How company executes complex co-ordination functions involving both internal and external resources?
- How it develops critical networks and learns within its community?
- How its people communicate and collectively foster a social sense of identity?

The importance of these skills increases, when resources must be coordinated in multicultural teams of multinational organizations within diverse national cultural framework. This knowledge is almost impossible to copy by competitors, it can only be gained through experience. Its uniqueness is derived from the co-ordination mechanisms, which operate in diverse cultural barriers, and are only valid within a holistic perspective. This includes the knowledge itself and is surrounded by cultural symbols, metaphors and norms. All this is captured by the notion of the Greek expression called *gnosis*. In case of companies, this *gnosis* provides the pragmatic skills and knowledge, which every firm has to possess to stand the fierce competition and the cultural environment, in which the firm experienced under which conditions the knowledge works. This *gnosis* cannot be benchmarked it must be learned the hard way. (It is not coincidental that companies with decades of international operational experiences seem to face less cross-cultural problems than their Japanese and Korean competitors.)

### **4. The Effectiveness of Multicultural Work Teams**

Multicultural teams are not all that successful one might expect. In the following section we have gathered comparisons on what kind of work tasks multicultural groups could be used for effectively. The opportunities for the different timing and objectives for the use of multicultural groups are shown on Table 2.

	EFFECTIVE	INEFFECTIVE
TASK	<i>Innovative</i>	<i>Routine</i>
STAGE	<i>Divergence (earlier)</i>	<i>Convergence (later)</i>
CONDITIONS	<i>Differences recognized Members selected for task-related abilities Mutual respect Equal power Superordinate goal External feedback</i>	<i>Differences ignored Members selected on basis of ethnicity Ethnocentrism Cultural dominance Individual goals No feedback (complete autonomy)</i>

Adler, 1992, p.135

Table 2.: The Effective Managing of Diversity in Work Groups

Table 3. summarizes the stages of the development of work groups and demonstrated the special features of multicultural teams.

STAGE	<b>PROCESS</b>	<b>DIVERSITY MAKES THE PROCESS</b>	<b>PROCESS BASED ON...</b>
<i>Entry: Initial group formation</i>	<i>Trust building (developing cohesion)</i>	<i>More difficult</i>	<i>Using similarities and understanding differences</i>
<i>Work: Problem description and analysis</i>	<i>Ideation (creating ideas)</i>	<i>Easier</i>	<i>Using differences</i>
<i>Action: Decision making and implementation</i>	<i>Consensus building (agreeing and acting)</i>	<i>More difficult</i>	<i>Recognizing and creating similarities</i>

Adler, 1992, p. 13

Table 3.: Diversity and the Group's Stage of Development

## 5. Experiences of Multicultural Projects-The Hungarian Perspective

A research has been done, which considered multicultural projects in Central-Eastern Europe in different segments of business. Hungarian regional headquarters or subsidiaries of the given multinational companies managed the projects. In-depth personal interviews were made with members of the projects on the advantages and challenges of working in multicultural teams. The same list of questions was asked from the interview participants. The research has been done at five different companies in Hungary. (Banking, copper industry, FMCG, paper industry and air transportation.) Companies and organizations were all operating on the international and some of them on the global level. Most of the team members of the projects under discussion were mainly from Central-Eastern Europe (Czech Republic, Hungary and Poland) the others were from Germany, UK, Indonesia,



Turkey, Russia and Norway. All of the multicultural projects were on research and development projects or on green field investments, therefore have relevance for the academic field as well. The following reasons were identified for cross-cultural conflicts:

- Conflicts due to power differences between the team members (headquarters vs. local partners)
- Conflicts due to historical stereotyping, which still affects negotiations and business
- Conflicts and misunderstanding due to the different level of language skills or the knowledge of a different foreign language as a third language as the language of the given project
- Conflicts due to communication problems, which result from the different context people, are communicating. The question of implicit and explicit communication. How to actually get valid information from other team members.
- Conflicts due to the different understanding of time and deadlines.

Based on the interviews we grouped the cultural challenges of multicultural projects into the following categories:

### ***5.1 The Achilles Heel: Communication Problems***

Whatever the chosen language of the project team were the following communication problems occurred:

- The different level of project language skills
- The evaluation of team members based on language skills
- Misunderstandings caused by information channels
- The different level of information needs
- The necessity of written documents

Very often team members are judged merely on their language skills, professional skills are left hidden because of communication barriers. At first take one shared language seems an easy solution for communication. Experience shows that a third language is usually more effective than having some team members speaking their mother tongue.

On the other hand no e-mail or fax messages can substitute the power of face-to-face communication. The ever needed trust for the team cannot be reached via Internet.

The most significant difference in communication is rooted in the low context or high context characteristics of the given cultures.

### ***5.2 The Question of Time***

- Deadlines
- Punctuality
- Different rhythm of work
- Milestones of a project
- Change in schedule

One of the factors which can destroy the development of trust and fruitful collaborations in a team is the differences in the perception of time. In the planning process of a project everything seems smooth, but when it comes to the first milestones to fulfill, conflict level can rise high. Monochronic people would keep the schedules to the last breath – even if it does not make much sense anymore!- whereas polychronics would tend to think that there is a more flexible timeframe than the written plans. As the project proceeds the differences can grow more significant having polychronics strongly focused on the end result and less on the milestones, which is crucial for the monochronics. Also weekends and national holidays can have different meaning for the team members in multicultural teams.

### ***5.3 The Leader of the Pack: Role of the Team Leader***

- The possibility for open communication
- The unquestionability of the project leader
- Methods of conflict-handling
- The standardization of the leader-member communication

The perception of the team leader have a strong influence and the effectiveness of the team. Managing a multicultural team is a major leadership challenge, therefore calls for special skills. The management of a multicultural team needs even more fine tuning from the leader than in local business settings. Leadership intelligence is culturally challenged!

The leader should solve the dilemma of being in multiple roles based on the cultural differences on the perception and understanding of a leader in a team. Methods of situational management are strongly recommended in multicultural environment. Best practices of home might not be applicable in such settings.

### **Conclusions**

The aim of the study was to identify dimensions of culture which have a major influence on the effectiveness of multicultural work groups. In-depth interviews were carried out at five different companies having multicultural projects in their operation. After gathering typical conflict situations of the projects, we analyzed the possible cross-cultural roots. As a conclusion we have identified three cultural dimensions being responsible for most of the conflicts, namely communication problems, the perception of time and the perceived role of the team leader.

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## **THE PERSPECTIVE OF ETHICAL AUDIT**

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*There is a growing body of experiences in corporate social and ethical accounting, auditing and reporting. The emergence of varied terminology and differing approaches has been associated with this development. One of the reasons for organisations undertaking some kind of social and ethical accounting and auditing is fact, that it allows them to make claims about their openness, and hopefully about their sound social practice. The analysis encompassed the investigation of the role of ethical auditing. The future growth of the role of ethics within the corporate world will probably also increase the demand for the ethical auditing.*

### **The concept**

Ethical audit is “the process of measuring and analysing business operations, connected to the ethically sensitive topics” [5]. Ethical audit is one of formalised ethical institutions that provide the basic tools for the internal integration of ethics. Therefore it facilitates the consideration of the ethical aspects of corporate decision, and provides ethically reasonable corporate activities.

Ethical audit can be internal audit or audit with external experts. The main purpose of both processes is the evaluation of the goals connected to the stakeholders of the organisation. In case of internal audit a professionally and hierarchically heterogeneous group of people should be formed, that is directly depending from the management of the organisation, in order to keep its independence. The next level of the evaluation is the sector-orientated benchmarking. The ethical audit, performed by external experts, is increasing the efficiency and validity of the ethical efforts of the company.

Ethical audit is strictly connected to the satisfaction of the needs of measuring ethical performance in organisations. Several tools were developed to satisfy these needs, representing chronologically and geographically diverse development.

### **Measuring ethical audit**

Corporate ethical audit is the evaluation of corporations from ethical point of view, differing from other economic and financial evaluations. Ethical audit is not able to substitute economic and financial evaluation, it is only complementary tool. The ethical audit can also be decision criteria for various groups of stakeholders, such as employees, consumers, investors, etc. The subject of the audit is the company, as a whole, not only its products, services or employees (e.g. management) [3].

Tools of ethical evaluation of companies:

- **Corporate tests**

Corporate tests are measuring and evaluating the company from an independent viewpoint, unbidden, on the basis of certain criteria. The tests are focusing on the social and ecological responsibility of the company on the previously defined areas of operations. The results are publicised in a condensed format, providing assistance to the decisions of different market partners of the organisation.

Ethical corporate test are evaluating the companies based on different criteria. An important example is the criteria system of "Shopping for a Better World". In the majority of the corporate tests the basis of the evaluation of the sustainability of the vision [6].

Usually the aspects of the evaluation are: does the company support charitable events, does the company have money in weapons, nuclear energy, how does it relate to racial questions, minorities, child work, environmental protection, animal tests, does it build flats to its employees, does it support local municipalities, how does it handle women and elderly people. The charts usually are not judging the company; the final qualification is left to the consumers or investors.

- **Indices**

Analogue to the financial ratios, the goal of indices is to measure the ethical performance of the companies. These indices show the results of ethical audit, and fit in to the system of corporate performance ratios. Several indices were developed in Hungary, as well.

- **Social Reports and Ethical Accounting Statements**

In the late 1980s new ethical systems have appeared, that were prepared to a leading company. For instance, Ben&Jerry's has introduced the yearly "Social Report" in 1998. This report has evaluated the ethical performance of the company on the basis of stakeholder interviews. The "Social Audit" of "The Body Shop" represented an external ethical audit. The basis of "Ethical Accounting Statements" of SBN Bank was the active contribution of the stakeholders [8].

- **Social/ecological/ethical balance sheets**

In order to lay the methodological foundations of ethical audits, the need for social, ecological and ethical balance sheets has appeared. These balance sheets are summarising the consequences of corporate acts to stakeholders. As it is considering several aspects of social legitimacy, ethical balance sheet can be more extensive than social or ecological balance sheet.

The previously mentioned examples underpin the success of SEAAR (Social and Ethical Accounting, Auditing and Reporting) movement, since broad legitimacy could have been achieved in several cases through the dialogue with the stakeholders [12]. The German and French counterexample of SEAAR, the social balance sheets, have

stalled at the level of a certain technocrat bookkeeping mentality, therefore they are not really able to spread in the corporate world [11].

The next step in the corporate evaluation of ethical performance was the development and application of standards. The basic foundations of the ethical evaluation are more often those structures or processes that allow legitimate solution for the conflicts.

**Ethical standards**

The ethical performance of the company can be characterised by standards that were not primarily developed for evaluating ethical performance. Gonella, during the analysis of social performance measurement and evaluation, has classified the existing standards and agreements as process-orientated or measuring fixed criteria, and concentrate on certain stakeholder groups or each stakeholder (Figure 1).

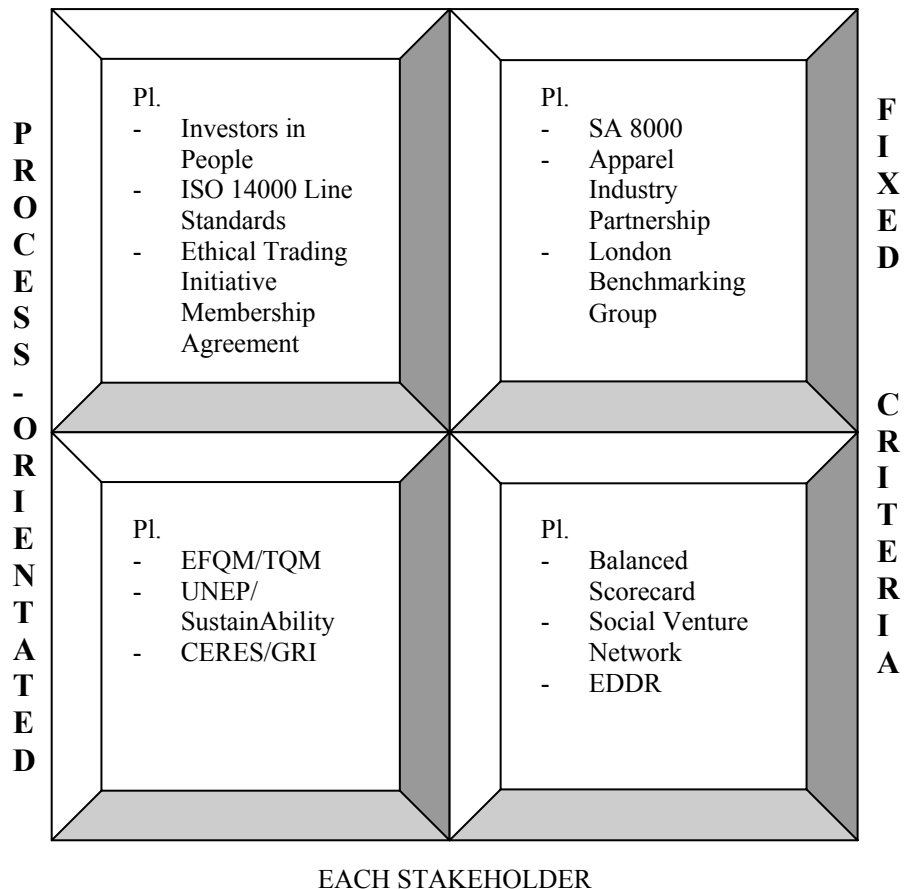


Figure 1.: Classifying standards and agreements [4].

From ethical point of view, applying ISO 14001/EMAS standard is prominent, as its goal is to protect the environment, therefore it is standing for the legitimate interest of the future generations. The standards for healthy and safe workplace conditions are standing for the interests of the employees. Despite the importance of the question, no international standard exists, only national or industry standards. The most popular standard, the ISO 9000 line is a quality standard. Its spread is the consequence of the market pressure and strategic necessity. Quality provided to consumers is not based on ethical considerations, although it has ethical importance, as the consumers are establishing a legitimate claim to high quality products.

Standards are certain organisational and behavioural rules. Their corporate adherence are audited by an independent institute. Those ecological or social organisational and behavioural rules are not considered as standards that are ordered by law or internal codes (e.g. behavioural code, ethical code) [9].

The primary goal of corporate ethical standards is to provide organisational and behavioural rules to the company, in order to consider the corporate ethical issues, and reach the corporate ethical goals.

Similarly to the example of ISO 9000, these standard involve the setup and implementation of a management system, that is regularly audited and certified by accredited external auditors.

In the following, three strictly ethical standard is presented: SA8000, AA1000 and Value Management System of German “The Centre for Business Ethics (ZfW)”. Based on the definition of standards, AA1000 and Value Management System can be primarily considered rather an ethically motivated auditing and reporting standardising experiment than a standard.

### **Social Accountability 8000 (SA 8000)**

SA 8000 was prepared by a non-profit organisation, Council on Economic Priorities in 1997. Currently it is belonging to Social Accountability International (SAI) institute. The standard is primarily including specifications to the rights and workplace conditions of employees, such as banning child work, taking into consideration of safe and healthy workplace conditions, freedom of movement and assembly, banning racial, sex, origin, religion or political discrimination, restricting working time and minimum wage specification.

These are primarily rules and regulations that exist in the majority of the countries, and are based on international regulations. The main difference of SA 8000 is the concept that certain rules, not implemented by corrupt or weak governments, are controlled and observed by companies. Another significant issue of the standard is observing the local law.



The corporations receive certificate for the observation of the standard, declaring that the company fulfils the requirements of SA 8000 standard. Furthermore, merchants may join the standard.

SA 8000 was introduced by major international companies. The partners of the project are OTTO Agency (Germany), AVON (USA), Toys R Us (USA), SGS (Switzerland). The members of the project should publish a report on the goals and development. The companies are audited in every three years. The audited companies are controlled in each six months. The control is performed on the basis of the auditing procedure of SAI. Auditors are accredited by SAI.

SAI has received 1 million USD subsidy from the U.S. Government and 0.6 million USD from the Ford Foundation. The number of certified producers has reached 66 in April 2001, primarily from textile and toys industry [9].

According to the assessors, the audited companies are expecting significant financial advantages from SA 8000, the corporate image is improving and the companies are able to avoid the attack of consumer movements.

#### **AccountAbility 1000 (AA 1000)**

AA 1000 was developed by Institute for Social and Ethical AccountAbility (ISEA), as a result of a two-year long international consultation process. AA 1000 is primarily focusing on Social and Ethical Accounting, Auditing and Reporting (SEEAR), i.e. the definition of ethically important issues in the organisation, ideally audited by external auditors, and followed by the publication of the results. AA 1000 is carried out according to strictly defined rules. The main concept is based on stakeholders, i.e. the organisation should secure its legitimacy through stakeholder involvement.

AA 1000 is a process-orientated system, described in Figure 2.

The procedure has five main processes, including several subprocesses (Table 1.):

1. Planning
2. Accounting
3. Auditing and Reporting
4. Embedding
5. Stakeholder engagement

Process	Subprocess
Planning	<ol style="list-style-type: none"> <li>1. Definition of processes</li> <li>2. Identification of stakeholders</li> <li>3. Identification of values</li> </ol>
Accounting	<ol style="list-style-type: none"> <li>4. Identification or evaluation areas</li> <li>5. Identification of the scope of processes</li> <li>6. Identification of indicators</li> <li>7. Information gathering</li> </ol>

	8. Analysing information, defining goals, finishing development plan
Auditing and Reporting	9. Preparing reports 10. Auditing reports 11. Publicising reports and collecting feedback
Embedding	12. Integration of system
Stakeholder engagement	13. No assigned subprocess

Table 1.: Processes of AA 1000 [1]

In this model, from ethical point of view, autonomy is highly important. AA 1000 is providing autonomy to the users, therefore it is not necessary to keep the rules. The processes should be primarily observed as a guidelines. If any inconsistency occurs, the focus is on our long-term goal: the accountability.

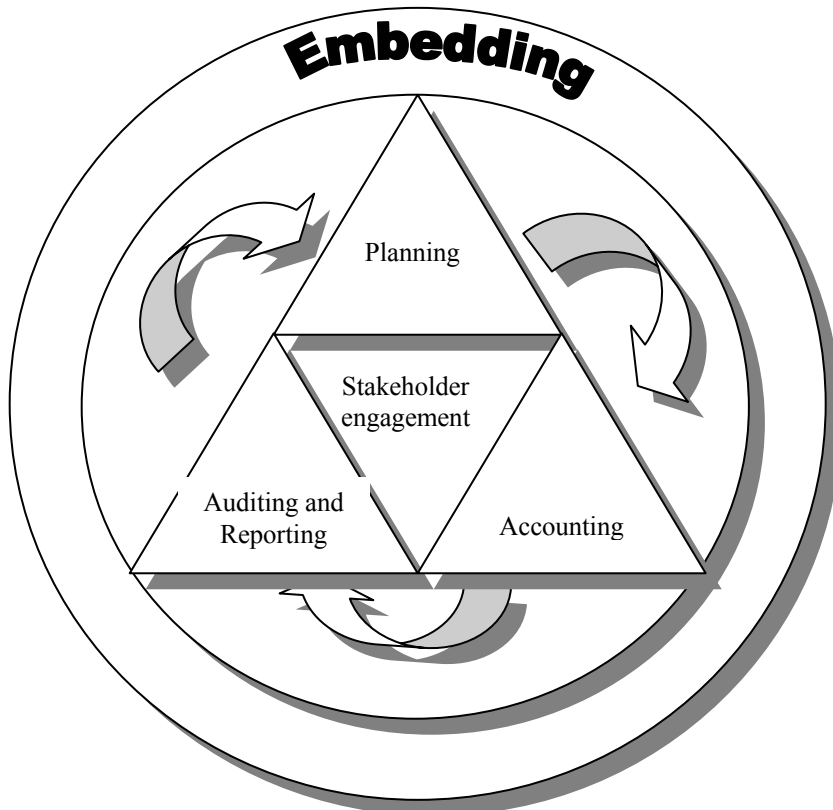


Figure 2.: Details of AA 1000 system [1].

**Value Management system for sustainable management  
(WerteManagementSystem<sup>ZfW</sup> für nachhaltige Unternehmensführung)**

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This system was developed by “The Centre for Business Ethics (ZfW)” in collaboration with the leading German corporations and associations in 1997. The major founders are: ABB, BASF, Fraport, Novartis and Siemens. The special feature of the system is that is focusing on the special characteristics of the European and German corporate culture. The goal of the system is to secure the sustainability and sustainable successful operation of the company.

The system is based on voluntary commitment. The main purpose of its introduction is not the prohibition of the defective operations, it is rather a continuous learning procedure. During this procedure the ethical requirements are intended to appear in the operations of the company. The system is involving all of the stakeholders. It is based on voluntary obligation and self-check, although it is possible to perform external audit. Auditing is meaning process monitoring. The elements of ethics management system, to be precise, the areas with hidden values, are revealed by interviews and questionnaires. The certificate shows that the audited company is operating ethics management. No ethical evaluation is performed.

The introduction of the system is a four step process:

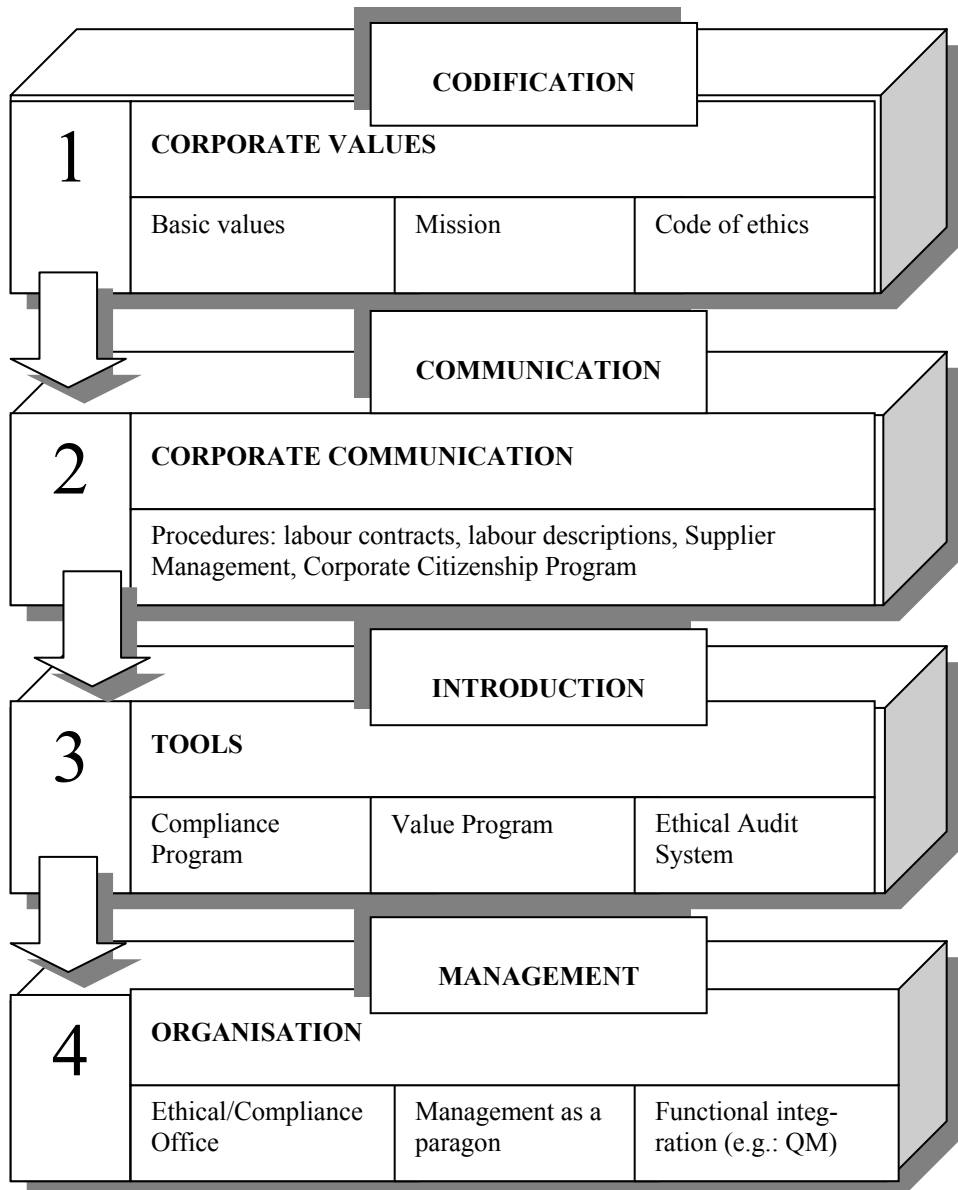


Figure 3.: Parts of Value Management System [7]

**Future trends of ethical audit**

Within the practical integration process of the corporate ethics, different stages could have been identified. In the beginning the experts were focusing on starting ethical programs, but these programs were found to be unsuccessful. As a next step, the primary goal was to build an ethical corporate culture, focusing on continuous development, instead of temporary programs. Currently the main emphasis is on the process of practical integration. The ethical aspect are not embedded in the corporate decisions, ethics should be managed.

The evaluation of the ethical performance is focusing on the processes that will secure or may secure the emergence of an ethical company. The standards, proven to be successful in quality and environmental management, are driving the organisations towards a process-oriented standard system, even on the field of business ethics.

Connected to the current standards, two major problem areas can be identified. The first problem is that these standards are not covering each stakeholders groups, the second is that they are not recognised internationally. The possible development options are the following:

- The international spread of the current, primarily ethical standards. The main barrier of this option is the fact that these standard were initiated by private institutes, and their introduction requires significant financial resources. SA 8000 does not cover all of the stakeholder groups, and it seems to be the standard of the larger international organisations.
- Amendment and unification of the currently used quality, environmental protection and security standard, originating an integrated standard. But the integration and harmonisation of the currently existing standard system is not an easy assignment. The existing and certifiable norms are usually not developed from ethical motivations. Although these standard are dealing with different stakeholder groups of the organisations, is can be questioned, whether they are appropriate tools.

It seems, that the future is not the development of an integrated standard, but developing an internationally recognised new standard. The International Standard Organisation (ISO) and the Ethics Officer Association (EOA) has started the development of a new ISO standard. This standard would allow the evaluation and communication of the corporate ethical initiatives and programs to each stakeholders group. The "Business Conduct Management Standard" would be a process orientated, guideline defining standard that could be introduced by any size of company, in any business area, and it would not necessarily be connected to external auditing. One of the main advantages of this standard, that it would be developed as a result of a consensus, and the reputation and worldwide familiarity of ISO would secure the spread of this standard.

According to the practice, significant changes are required, in order to improve the ethical level, to build responsible, ethically sensitive organisations. The changes

should be started at the foundation of the organisations: the personal values and the economic theories. Unfortunately, these are the most difficult steps. We may achieve the result faster with the “policy of smaller steps”. The main tools of this policy can be the ethical institutions. According to the empirical researches, in case of the majority of the companies, the main cause of the emergence of ethical aspects is primarily the force of different stakeholder groups. These groups are considering the introduction of ethical aspects as a tool for the successful operation of the company. Considering this, ethical audit may be one of the most efficient tool to integrate ethical aspects into corporate decisions, systems and cultures.

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## **THE BASIS OF THE CORPORATE IDENTITY: CORPORATE PHILOSOPHY AND PERSONALITY**

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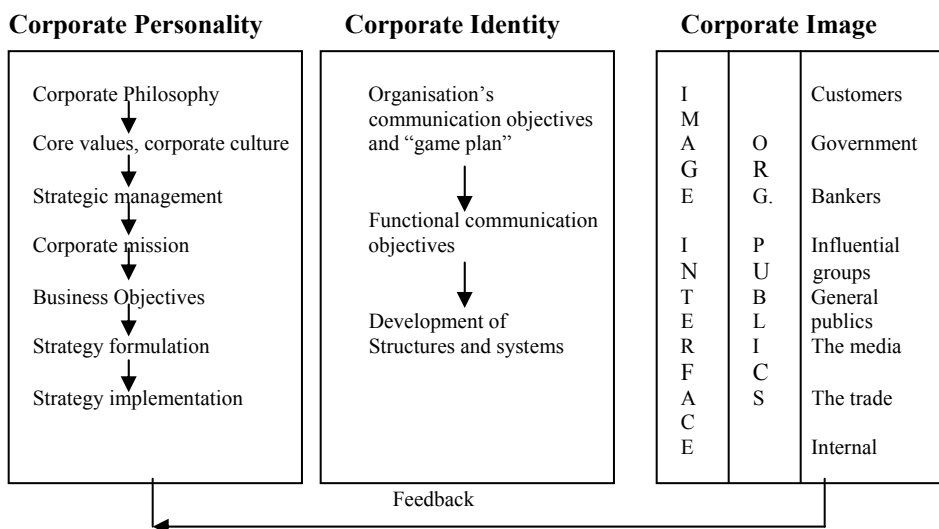
Corporate Identity has many definitions, it encompasses a broad range of disciplines and it means many things to many people. The International Corporate Identity Group recognises that it is inappropriate to impose a rigid definition of what Corporate Identity is. (ICIG Statement On Corporate Identity, 1996) This paper, therefore, does not intend to define this term.

The term has become familiar with professionals, and it is gradually penetrating even into the minds of the wider public. It is generally used in relation to business entities or manufacturing companies, however, it can describe also the identity of a non-commercial organization, association, region or event. It covers the basic features of any entity or organization. (Jašo, 2000) These features are its history, "personality", philosophy, values, principles, core message, its mission and its vision.

Corporate Personality and Corporate Identity are inseparable concepts. Wally Olins is said to be the first who suggested this in his first book "The Corporate Personality: An Inquiry into the nature of Corporate Identity". Furthermore, he stated that of all concepts in use in the are the Corporate Personality is the most important. (Balmer, 1997)

The relationship between Corporate Identity was best describe by Abbratt's famous definition: "Corporate Personality) is defined as the total of the characteristics of the organisation. These characteristics serve to distinguish one organisation from another. The personality is projected by means of conscious cues, which constitutes the identity. The overall impression formed in the minds of audiences constitutes an image..." (Stewart, 1991)

His following model establishes the main relationships between the key concepts:



The objective of this article is to introduce the internal aspects of companies: the espoused corporate philosophy and the hidden or deliberately espoused personality, both parts of the "Corporate Culture" element in many CI models, on which the identity is based.

### Corporate Philosophy: Assumptions, Values and Mission

Various authors suggest that the starting point of examining the determinants of the identity is looking at the *corporate philosophy*, which follows from the corporate purpose, i.e. what the company stands for. Stevenson (1991) defines philosophy as "the *values and beliefs* which a company holds and which *drive its corporate activity*". As a result of the basic assumptions, values, ethical standards and the subsequent mission the company develops a personality which is "the set of characteristics which make a company that company and *distinguishes* it from others" (Stevenson, 1991) Uniqueness is a key feature of corporate personality, says Bernstein (1984). It will ensure that the identity is also unique which helps to identify that organisation by its various publics and prevents from confusing it with the others.

Before looking at each of the philosophy components, the sequence of them has to be set up. Schein (1985) suggests that the deepest category is the 'basic assumptions' on which 'values' are based. The difference between these two categories is that assumptions are taken for granted, they are invisible and preconscious, whereas values represent a greater level of awareness. (Schein, 1985)

### Assumptions

Assumptions are the basis of any organisational culture. As Pascale and Athos put it (Dowling, 1993), organisational culture is the 'glue' which holds many organisations together and which helps explain differences in competitive effectiveness. The glue is



based on a set of basic assumptions which the members of an organisation take for granted.

Apart from the principles behind the assumptions, they can be grouped on the basis of being up-to-date or outdated, simply right or wrong. Shapiro (1991) argues that there are many assumptions which are usually acted upon by most of the companies without any revision, consequently leading them to wrong decisions.

What companies think about themselves, more exactly, what managers think about their company and what image is thought to be perceived by the public are also assumptions. Olins says that a CEO "knows what he *thinks* of his corporation better than anybody else, but he doesn't necessarily know it better". (Vogl and Weiss, 1991) The lack of knowledge makes managers base their decisions on assumptions. It is very general that a CEO says that the company has got an image or identity problem, however the problem might be more deep rooted. An example of this was a market research carried out by an MBA study-group, in which the writer took part, for a company which provided different kinds of business services in West Yorkshire. The brief stated that they had an image problem, however we ended up giving them recommendations concerning their organisational structure as well. In the course of interviewing various departments, one of them reported on successful business activities and the market research proved that their services were not favoured by their customers. They acted upon a wrongly held assumption.

Shapiro (1991) argues that some bad assumptions are artificially maintained by managers who support them so strongly that even counter arguments are suppressed or distorted. The existence of these processes might lead companies to widening gaps between what they are doing and what they should do, consequently they might get far from the identity that they ought to present in order to evoke a favourable image.

It is very important to know which assumptions in an organisation are to be maintained or to be get rid of since only the first category of assumptions should serve as a basis for corporate values

## **Values**

Values are defined by Armstrong (1993) as follows:

"...what is regarded important, expressed as beliefs on what is best or good for the organization and what ought to happen..."

This definition suggests that values are more than assumptions in that they are expressed, and group assumptions as bad, right and best. Schein (1985) divides values into two main groups:

1. Ultimate, nondebatable, taken-for-granted values, which are close to assumptions;
2. Debatable, overt, espoused values, that match the above definition of Armstrong.

Since values are of "greater level of awareness" (Schein, 1985), they can be formed and channelled, thus they are managed easier than assumptions when a company is to establish an identity. Values serve as a basis of the company's behaviour both internally towards staff and externally towards society (internal and external behavioural identity). Dr. Wolfgang Reitzle, ex-Member of the Executive Board of Directors, BMW AG, Munich, claims that the abundance of cultural values that prevails in BMW's own corporate behaviour, exerts an influence on the company's identity (Reitzle, 1992).

Deal and Kennedy (1982) argue that as the essence of the corporate philosophy for achieving success, values provide a sense of common direction for all employees and guidelines for their day-to-day behaviour. They spell out what the company is striving for. Such company norms can be profitability, efficiency, service to customers, technical excellence of product or service, care for employees, promotion possibilities, welfare funds, recognition of trade unions and much else (Donaldson, 1989), these values affect all aspects of the company, from what products get manufactured to how workers are treated (Deal and Kennedy, 1982). Some of these values form the basis of the internal behavioural identity (e.g. care for employees, promotion possibilities, i.e. how workers are treated), others support the external one (e.g. service to customers, technical excellence of product or service, i.e. what products are made). The strength and relative importance of these values will then determine which of them will dominate the company, which of them will mostly build up the corporate personality and thus contribute mostly to the identity.

Deal and Kennedy (1982) remark furthermore, that "values can powerfully influence what people actually do,...values ought to be a matter of great concern to managers. In fact, shaping and enhancing values can become the most important job a manager can do". The authors found that successful companies place a great deal of emphasis on values. In general, these companies shared three characteristics:

- They stand for something – that is, they have a clear and explicit philosophy about how they aim to conduct their business.
- Management pays a great deal of attention to shaping and fine-tuning these values to conform to the economic and business environment of the company and to communicating them to the organisation.
- These values are known and shared by all the people who work for the company – from the lowliest production worker through to the ranks of senior management.

Deal and Kennedy (1982) observed that many successful companies have a very rich tradition of values, beliefs, and themes that have developed over the years. These values mostly come from experience, from testing what does and doesn't work in the economic environment. But employees also have a strong influence in shaping the standards of the organisation, as opposed to those companies where "many of the people who have the facts don't (or can't!) speak up" (Shapiro, 1991). The latter companies might not be able to adjust their corporate behaviour to the changing environment. It will badly effect their presented identity: they say about themselves

that (1) 'we are slow moving, incapable of change', externally, and (2) 'we don't listen to our employees', internally. In the writer's experience, most of the state owned companies fall into this category in the East-European countries.

Strong value system results in strong personality, which, in turn, affects strongly the identity presented. However, there are two pitfalls of strong values. One is 'the risk of obsolescence', values that become 'old fashioned' compared to what the changing environment requires. The other is 'the risk of resistance to change', sticking to values even at the expense of losing out on possibilities of success if necessary changes are not implemented. (Deal and Kennedy, 1982) This is very often the reason why deep and serious problems are treated as only image problems rather than as identity or personality ones. Thinking in terms of the latter solution would require companies to challenge their values.

One subset of the corporate value system is the ethical codes formulated by a company, which represent its moral values, the social responsibility the organisation has to present both internally and externally. The Cummins Practice on Ethical Standards sees ethics as resting on "a fundamental belief in people's dignity and decency" and states:

"Our basic ethical standard is to show respect for those whose lives we affect and treat them as we could expect them to treat us if our positions were reversed." (Donaldson, 1989) This is a clear expression of what is called the Golden Rule.

Mainly companies aim at solving the dilemma: how to keep the business responsibilities in respect and at the same times remain profitable. This is best exemplified by one of the ethical codes of Unilever, quoted by Donaldson (1989):

"We never forget that our most important single responsibility is to keep Unilever profitable. Without profit we cannot discharge our obligations to shareholders, suppliers, customers and employees. Unilever's ability to create wealth in developed as well as developing countries increasing-ly depends on an understanding that our operations are beneficial to the countries concerned and that our behaviour is of the highest standard."

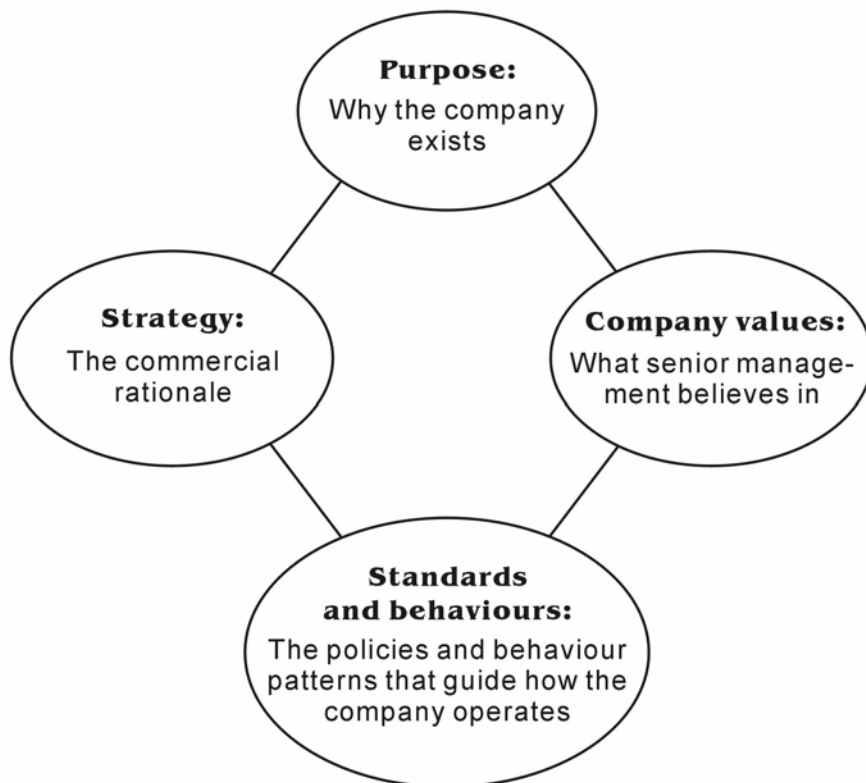
The problem of being ethical or achievement oriented exists on the individual level as well. Weeks and Nantel (1992) points at the fact that "business people in general, are faced with numerous ethical dilemmas and pressures to compromise their personal ethics to achieve corporate goals".

Values, including ethical codes, are expressed clearly, in most of the cases they are written. They can thus affect the corporate image in two ways: directly, the communicated set of values and standards, mainly in the form of mission and value statements, make impressions, e.g. Unilever is a profit oriented company whose

foreign business conduct is highly ethical or, indirectly, through influencing the behaviour of the company, i.e. through its behavioural identity.

### Mission

Assumptions are thought, values are expressed and mission is focused and written in the form of a mission statement. Focusing means concentrating on certain areas of company activities, e.g. employee care, quality, customer care, environmental and social issues, relationships, and they are targeted to different groups of the society, accordingly. Mission is made to be an easily comprehensible manifestation of corporate values and beliefs. There is a broader definition of mission, introduced in the Ashridge Mission Model (Campbell and Tawadey, 1990) below:



The Ashridge Mission Model

The starting point of corporate philosophy is the purpose of the company, in the same way as the above model puts it to the first place. The result is the set of behavioural standards and actions into which the purpose and strategy are converted. This is exemplified by the following quotation about The Body Shop:

"The Body Shop...has a purpose of developing cosmetics that do not harm animals or the environment. Its strategy is to be more environmentally conscious than its competitors, hence attracting the 'green' consumer and the 'green' employee. Environmental consciousness within the company has been translated into policies and behaviour standards...All employees have two wastepaper baskets: one for recyclable and the other for non-recyclable products. employees receive training in what they can be recycled and in what cannot." (Campbell and Yeung, 1990)

The example of The Body Shop shows clearly how the original purpose and values can become behavioural standards presented as behavioural identity to the society. The Body Shop is "against animal testing". This is one of their values, it is stated as a mission, it has become part of their strategy, they educate their employees and the society to accept it, the appearance of their brands carry the message, it is part of their corporate advertising and the message is put through several communication channels.

The corporate mission is manifested and communicated in the form of mission statements, sometimes called as the 'credo' of an organisation. Pearce (1982) lists six components of mission statements:

- product or service, market and technology
- goals for survival, growth and profitability
- company philosophy
- company self-concept
- *public image*, and
- responsibility to stakeholders

From the point of view of the topic of this article, 'public image' is held the most important in the list. Pearce remarks that customers attribute certain qualities to a particular business (Campbell and Tawadey, 1990). These attributions can be favourable or unfavourable for a company. If the public image is negative it often makes firms re-emphasize the beneficial aspects of their character and as reflected in their missions. These new missions are then form basis of an identity change which is aimed at bringing about a new image in the public.

Statements of mission should have a personality, say Campbell and Tawadey (1990). They should be unique. The most regarded statements were those that reflected the personality of the organisation. The next section is about the corporate personality.

### **Corporate Personality**

According to Olins, corporate personality is the soul, the persona, the spirit, the culture of the organisation (Olins, 1978). Its presented form is the identity. The personality encompasses the various characteristics of the organisation, therefore, it could even be called the character of the company, which is the outcome and distilled result of the whole set of assumptions and values. Uniqueness and distinguishability

are key features of personality. If the corporate personality is unique and distinguishable, so will be the presented identity. Or, vice versa, no identity can carry the above two features if the personality does not have them.

Usually, in the subsequent period after the establishment of an enterprise, the personality of the company is equal that of the founder (Olins, 1978). Colin Chapman of Lotus and Jack Cohen of Tesco are good examples. When the business is getting out of control of the founder, either because he retires or the scope of the business becomes too big, the personality of the company is increasingly determined by only the abstract corporate philosophy. The task of the company, therefore, is to prepare for the later stage, when the, by that time developed system of assumptions, values and mission statements, take over the role of personality determination.

An organisation has got a clear, presentable personality if all its determinants consistently follow each other, there are no acute contradictions in the company's assumptions and value system, which make the personality and consequently the identity blurred. That is why the company should never stop at saying that it has an 'image or identity problem', it has got to go deeper. Bernstein (1984) suggests that companies should find out what their personality is by means of research, both internally and externally. This has led the writer suggest that the public image, result of the whole self-presentation process, should feed back into the personality.

The corporate personality often takes the form of a statement in annual reports and other brochures and composed as human characteristics. The example of this is taken from Provident Financial:

"PERSONALITY

(A summation of the personality characteristics which makes an organisation what it is.)

Not an easy person to get to know – but worth the effort.

Shrewd, with a quiet confidence born of long years of success. Exploiting opportunities where other may see none.

A product of his birthplace, he epitomises its values. Down to earth. No nonsense. Plain speaking.

He does not suffer fools gladly.

He is not impetuous but once he has made a decision he acts quickly.

Though conditioned by its heritage, he is not its prisoner. He is forward-looking and youthfully eager to find fresh applications for his expertise. But he will not venture beyond his competence.

If he were a G.P. he'd be hardworking (from a medical family) in a modern practice who tells you the truth because he has no time for anything else. His patients may not like his bedside manner but they trust him. They know him.

And he knows them." (Communication Guidelines of Provident Financial)

Personality, which expresses the characteristics of the organisation based on its beliefs, assumptions and values is the answer to the implicit question: 'Tell me who

you are'. But the public asks more: 'Show me who you are. Show me how you express yourself by your behaviour and by the way you look'. The company, obviously wants to answer these questions as well.

This answer is called the CORPORATE IDENTITY.

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## **A FORGOTTEN FACTOR OF THE COMPETITIVENESS OF HUNGARIAN ECONOMY**

### **PROBLEMS OF REFORMS OF HUNGARIAN LOCAL GOVERNMENT SYSTEM**

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*A substantial achievement resulting from economic and political changes in Hungary has been the development of the local government system. That sector has a key role in the absorption of the funds from the European Union, and the competition of regions for the investors. In spite of some undoubted achievements in the local government system, it can be stated that one of the bottlenecks of the accession process is actually the local government sector. This paper is meant to analyse, from the perspectives of economics and finances, the experiences in the operations of the local government system in Hungary and make recommendations as to some possible further development options thereof. The main findings are that the Hungarian situation could be characterized as a decentralised system without subsidiarity which calls for fundamental reforms. The study includes data on the Hungarian local government sector, and an international comparison.*

This study, which examines the role of subnational public sector in competitiveness of the Hungarian economy, including an analysis of the present state of the Hungarian local government system, has six sections. The first gives a general theoretical background on relationship between economic competitiveness (including regional competitiveness) and performance of public sector. The second is a general overview of the Hungarian local government system. The third provides an analysis on financing Hungarian local governments. The fourth section presents an evaluation of performance of the previously described system. The fifth shows the challenges of globalization and the EU accession for the Hungarian local government sector. And the last one gives scenarios for possible reforms.

#### **1. Competitiveness and the public sector**

Competitiveness, as a notion, has become the focus of attention in applied economics for nearly twenty years. Economic sciences have always studied with various intensity the components of competitiveness; take for example the theory of

competitive advantage by David Ricardo, or the theory of innovation by Schumpeter, or the theory of growth by Solow. In the 19th century it was Karl Marx and Friedrich Engels who put emphasis on the non-economic factors influencing competitiveness. Defining the notion of competitiveness itself is fairly difficult since it cannot be traced back to any economic paradigm (TÖRÖK 1999. p.25) To add to this finding one can say that all economic theories, except the classical Marxist economic theory, have neglected to study the link between the economic and other social sub-systems even though competitiveness is a complex phenomenon defined by economic-, social- and cultural factors.

Competitiveness means the readiness for competition in the market. This term can be interpreted on microlevel, i.e. on company level, on mezzo level, i.e. regional level, on macro level, i.e. national level, and on international level, i.e. globally. The indices that show competitiveness on micro level are profitability, market share, acquiring and sustaining market position. On mezzo (e.g. regional) and macro (e.g. national or Community) level the main indicators are rate of sustainable economic growth, level of employment, and state of environment etc..

Those schools that study competitiveness either implicitly or explicitly deny the paradigm of a perfect market and are for state intervention. Consequently, the so-called microeconomic policy can be justified. By this term Ádám Török means the following: *"Those economic policy recommendations can be considered as microeconomic policy that influence the operation of the market and as a result of this, the actors of the market, not by the means of macrolevel financial processes but rather by legal sanctions or by non-taxlike direct financial transfers."*(TÖRÖK 1999. p. 22)

The theory of competitiveness distinguishes the competitiveness that of supply and demand because to measure and influence these completely different sorts of methods are necessary. The ultimate characteristic feature of the competitiveness of the supply side is the productivity level or its increase.

In 1965 R. Farmer and B. Richman summarised the factors of competitiveness in a four tier matrix. (IMD 2001, p.48). The four tiers are the political and legal factor, the education factor, the social and cultural factor and the economic and business factor. The latter one includes the business activities, e.g. planning, marketing and production policy.

Today's most dominating idea, first published in 1990, is that of Michael Porter's, professor of Harvard University, and is about the rhombus of competitiveness. It needs to be emphasized to support our point that just like Farmer and Richman, Porter considers the government as a competitiveness factor on its own. (PORTER 1993, pp. 48-49)

With the appearance of globalisation, out of the various factors of competitiveness, the role of a new factor has been appreciated. (PORTER 1998) Porter writes the

following: Paradoxically, in the global economy the long-lasting advantage in the competition of companies are strongly localised, which fact can be attributed to the concentration of highly specialized expertise and knowledge, institutions, competitors and demanding customers in a certain part or region of a country. The density of geographical-, cultural- and institutional conditions make not only the individual access possible, but they also provide special connections, better information, stronger motivation and other opportunities that enable to increase the level of productivity, that can only be exploited locally. Local matters seem to appear in a completely different light at the turn of the 21st century.

Regional competitiveness could be measured as the amount of income per capita produced in the region and the growth rate which relies on work productivity and high level of employment. In other words, competitiveness is such sustainable economic growth which is a result of high level of employment and high level of productivity. Consequently, there's a strong correlation between the regional economic growth measured in GDP, work productivity and level of employment; the change of any of these will change at least one other factor.

### ***1.1. Local Governments as key factors of regional competitiveness***

However, it is not only Porter who mentions the defining role of the different levels of the government. The World Competitiveness Yearbook, which has been published year by year on the basis of a comprehensive statistical analysis by the International Institute for Management Development (IMD) mentions two factors of competitive input concerning directly the authority of local governments. (IMD 2001, pp. 48-49) To measure the competitiveness of a country the World Competitiveness Yearbook uses altogether 8 factors of competitiveness, and they are analysed using 290 criteria. The factors are as follow:

- domestic economy
- international integration of the economy
- government
- financial system
- infrastructure
- quality of management
- science and technology
- human factor( IMD 2001, p.54)

In the methodology of IMD the government as a competitiveness factor is described with 46 criteria. Besides this, the factor of infrastructure must be mentioned which is described with 37 criteria, and on which the local government has influence, or bears responsibility of provision, such as utilities, renting real estate, human infrastructure, health care.

With the appearance of regional competitiveness, the hypothesis by Tiebout has been put in a new light. The Canadian economist, Tiebout, after studying the services of public goods and the advantages of fiscal decentralisation came to the conclusion that consumers (citizens) of the local public goods can manifest their preferences by

choosing their residence. Tiebout concluded that actual operation of local governments show analogue with the operation of the competitive economy.

In Tiebout's system of ideas he made the following presumptions:

1. The consumers of local public goods can move freely and can choose the preferable local government as a residential place.
  2. Consumers are fully informed about local taxation and budget, that of the local utilities, and as a result of this they move between places of residence.
  3. They can choose from a great number of local governments.
  4. It is not necessary that the place of living and the place of work coincide.
  5. Local governments impose poll tax to finance the expenditure programs.
  6. There is no spillover effect.
  7. The average cost function concerning the residents financing the expenditure programs takes a U-shape.
  8. Communities can attract new inhabitants to reach the optimum level of size.
- (TIEBOUT, 1956; BLANKART-BORCK, 2000)

Let us notice that out of these presumptions the poll tax equals the spread of the costs of local public goods, while the lack of overflow means the concept of treating the local governments as clubs.(ed. PEARCE, W.D., 1993) The mechanism of "foot voting" results that taxation that finances local services can be harmonised with the preferences concerning public goods on both individual level, and both on the level of other participants of the economy. If migration is possible, and this is another condition to be fulfilled in the mechanism, then the individuals as well as the companies move to the area where the local government provides the preferred tax and service combinations. The competition of local governments causes several favourable effects. It results in a better and more efficient fulfillment of tasks and more efficient division of resources among local governments. This concept mentions another effect, i.e. in the field of public services local governments can compete with other levels of the public sector. This theoretical approach seems to be analogue with the concept of a perfect capital market. According to this concept, in case of certain conditions, any participant of the economy can count with the same financing costs. But this is in contradiction with the presumption in which the costs of public goods can be shifted from one generation to another by using various capital market instruments. This can guarantee the accomplishment of the utility principle of taxation with not only by the geographical spread of burdens of public services, but by the different generations sharing the costs. Naturally, to fulfill completely this hypothesis several conditions must coincide. It is not by chance that the concept was born in North-America and most of its followers can be found there. Their public finances, including that of local governments', and the structure of their economy are the closest to the requirements to make the model operational. However, three critical points must be mentioned when one talks about the Tiebout model. Firstly, because of the definition of pure public goods the U-shaped average cost function cannot be interpreted because the threshold cost is zero when a substituting consumer enters. One-amount local taxation does not seem to work in practice. Wealth tax and income tax might have several distorting effects. The third point is the difficulty of mobility,

or the limited number of local governments to choose from. To make the picture more thorough- and this can be accepted as a distorting effect on the market mechanism imagined by Tiebout is the fact that the USA spends a significant part of its GDP on equalising the regional disparity and the existence of a subsidy system contradict the operation of this model. According to Tibor Palánkai, from the budget of the European Union, 0.4% of its GNP is spent on equalisation of the regional disparities as opposed to the US or Australia, where this figure is 3-7%. (PALÁNKAI, 2003) Neither the Community budget system nor the mentality make such system operational. What's more, the declared aim of the regional policy of the EU is to equalise the regional disparities. But one has to admit that some operational elements that prevail in the model can be seen partially. Globalisation is accompanied by the appreciation of the locality and the role of towns and it changes the economy from a geographical point of view. Instead of regionalisation the appearance of networks can be noticed. Towns have become the basic units in economic space. Because of the liberalisation on the rules of capital investment and because of the easing of its technical limits, towns, especially bigger towns, literally compete for the capital investments of multinational companies. At the same time, the most crucial moment concerning the competitiveness of multinational companies is the choice of their premises, i.e. the optimal placement of the network in space. The generator of economic development nowadays is the so-called non-visible resources. Such special resources might be the entrepreneurial environment ready for new innovations, the technical-technological culture, the qualified and flexible work force and the supporting backup services.

The competition between towns has appreciated competitiveness and town policy that conduces competitiveness. In regional competition towns and their agglomerations have key roles. In their development concerned groups try to seize and sustain advantageous positions. The role of the local economic policy is to generate new jobs by the mobilization of the non-visible resources and by the development of the companies' willingness. The conditions to realise these efforts are the co-operation between the local authorities, the local economic lobby groups and the civilian sphere. This type of competition shows analogue with the mechanism presumed by Tiebout. With certain constrains the effect can be seen in various countries. Thus, the competition between towns can also be seen in Hungary, of which tools are the developments of towns and incentives for investment. The establishments of industrial parks, tax exemptions of businesses and the newly established construction areas around bigger towns and in the agglomeration of the capital have all changed the economic structures of Hungarian towns and the components of their inhabitants. The competition of towns stimulates the innovative activity of the public sphere and the more efficient utilisation of local features. At the same time it has to be mentioned that because of the limited number of participants and because of the political basis of decision making the competition is restricted. What I disclose is that the local government sector has a key role in the Hungarian economy concerning its global competitiveness. This role mainly appears through the economy's ability to absorb capital. It must be emphasized that here the role is not of the local governments' but that of the whole system's.

Applying the previously introduced term of regional competitiveness the effects of the local governments on competitiveness can be collected in the following main fields:

- having strong social cohesion; the ability to deal with various conflicts, such as employment, migration, crime etc., and the willingness of various local governments to co-operate
- quality of environment, both natural and man-made
- qualified work-force; human capital
- economic structure (processing industry, food industry, production, services)
- quality of public institutions, efficiency of their operation
- existence, structure and operational environment of small and medium size companies
- existence and operational environment foreign investment
- transparency concerning politics and local economy

## 2. The Fiscal Decentralization in Hungary

Hungary was one of the first transition countries to reform its intergovernmental system. The Constitution includes a guarantee that each local community has the right to local governance. Mandatory services to be provided by local governments can be mandated on them by *law exclusively*. In 1990 it enacted a fundamental law establishing local governments patterned on the basis of the Council of Europe's European Charter. The newly established local governments perform their administrative, official and public service provider functions with a relatively high degree of political and economic independence. The Hungarian Constitution and Law on Local Government define three economic bases of constitutional independence of local governments. Firstly, the right of levying local taxes and getting other own resources, funds. Secondly, the central government should transfer funds and share some central taxes to finance obligatory tasks of local governments. Last, but not least a huge amount of assets had been transferred to local governments. Property transfers to local governments gave them not only management rights on assets necessary for service provision but ownership rights as well. The process of dismantling state ownership has affected local governments in another way, since they received some of the proceeds from the sale of some state-owned assets in the competitive sector.

The Constitution does not make any distinction between local governments of various types. In Hungary there are municipalities (parishes, villages, towns, capital districts, cities), counties and the capital city, as a special regional local government. Thus, all players in the system, from the Capital City down to communities of a few people, are deemed legally equal. According to the Law on Local Self Governments, all actors of the system regardless their sizes have the same rights. However, that "de jure" situation becomes completely different "de facto" when it comes to actual service provision and financial management. The Law on Local Self Governments significantly scaled back the responsibilities of counties, which are the *regional bodies* of the system. These units have no right to levy local taxes. The system is based on settlements, without any coordination by law. As to the legal framework, it should be mentioned that a single-tier system was implemented. The Hungarian local

government system is fragmented. As a result, there are now approximately 3.200 local governments of which about 1.670 have less than 1.000 inhabitants. Table 1. shows the types of settlements and administrative units of Hungary and the Hungarian NUTS system.

Table 1: Types of Local Governments and Public Administration Units in Hungary under the NUTS<sup>1</sup> system

Capital city	Districts in capital city	City with county rights	Towns	Village	Parish	County	Total
1	23	22	229	187	2893	19	3187

Level	Description Limit in number of inhabitants (million)	Number of units
NUTS1	Large region 3-7	3
NUTS2	Development region 0,8-3	7
NUTS3	County (capital city) 0,15-0,8	20
NUTS4	Sub-region	150
NUTS5	Municipality	3135

This legal framework tried to adopt the general principle of subsidiarity. This principle says that public services should be supplied by the smallest unit of government that is administratively and economically capable. This process was driven in large part by an understandable political imperative to get rid of the old system but led to excessive *fragmentation*. At the same time the Hungarian local governments have a wide scale of responsibilities. Local governments are obliged to provide primary education, basic health and social welfare provisions, safe drinking water, waste disposal, public lighting, and to maintain local public roads and cemeteries. They are also obliged to enforce the observance of rights of national and ethnic minorities. Other competencies – not all mandatory – include providing local mass transport, settlement development, fire protection, public security and the explicit voluntary provision of cultural and sport facilities, housing and public safety. Table 2. shows a European comparison of the high degree of fragmentation of Hungarian municipal system.

<sup>1</sup> According to 1059/2003/EU Regulation

Table 2: Number of local governments, population, land size, and ratios in Europe (1992)

Country	Number of local governments	Land size thousand km <sup>2</sup>	Population million people	Population / local government thousand people	Land size/ local government km <sup>2</sup>
Austria	2.301	83,8	7,7	3,3	40
France	36.763	551,6	57,0	1,6	15
Hungary	3.148	93,0	10,3	3,3	30
United Kingdom	484	244,1	57,0	118,5	504
Germany	16.061	357,0	79,1	4,9	176
Sweden	286	450,0	8,5	30,0	1.437

In the past decade, no priorities of fiscal policies have been attached to public services provided by local governments. There have been obvious reasons to it. First, economic policy before 1996 had to be focused on the handling of the economic crisis that was associated with the transition, and on economic stabilisation. Secondly, each of the governments so far has done the reflex action of centralisation. However, when we think about problems like wastewater, environmental pollution, and boosting local businesses, then it is clear that those are strategic issues, in the solution of which the local level has a key role. The budget of the local government sector represents about 12 percent of the annual GDP. At the launching of the new system in 1990, its proportion in the GDP was 13.7 percent. That share was increasing for a few years. The high proportion can be explained by a dramatic drop of GDP, and an increase in the number of services “given down” from the central level to the local level. The local government sector receives 24 percent of the primary revenues of the general government, and spends 25 percent of the primary expenditures. Table 3. shows the expenditure of central and local government sector.



Table 3: Expenditure of the central and the local government compared to GDP (in percentage)

	1991	1993	1995	1997	1999	2001	2002	2003
Total value of GDP (Billions of HUF)	2 498	3 548	5 614	8 542	11 750	15 825	16.500	18.574
Share of the central government (%)	33,2	35,0	35,4	25,9	31,3	28,9	35	31
<b><i>Share of local governments of GDP using GFS approach</i></b>	<b><i>15,2</i></b>	<b><i>17,2</i></b>	<b><i>14,6</i></b>	<b><i>13,3</i></b>	<b><i>13,0</i></b>	<b><i>12,3</i></b>	<b><i>12,8</i></b>	<b><i>11,9</i></b>

Source: National accounts of Hungary and the annual financial reports

During the period analysed, the number of services mandated on local governments by the state has increased, whereas the funds allocated to the individual services have dropped. The, so-called, normative grants attached to various services finance two thirds or less of the cost of service provision on average. This shows that the decentralisation of service provision has not been accompanied by a parallel decentralisation of funds. A substantial part of the burdens and tensions associated with the reduction on service provision by the state has also been decentralised. That process is illustrated by the data in Table 4., which shows the real values of the expenditures incurred by the sector. It is clear from the data that the nominal expenditures of the local government sector have not kept pace with the increase in the consumer price index. This was the consequence of general fiscal restraint of Hungarian economic policy. A substantial decrease occurred in the real value of the expenditures of the local government sector; however, it was not a steady process. In 1992 and in the two years of elections (1994 and 1998), an increase in real value occurred from one year to the other. A drop in real value cannot be considered as a negative process exclusively. Restrictive funds distribution measures have helped many efficiency reserves surface themselves in the financial management of local governments. It can be stated for certain that the sector has still got additional efficiency reserves in it.

Table 4: Local expenditures in Hungary (1990-2001)

Year	Expenditures by GFS (HUF billion)	Nominal change (%)	CPI(%)	Change in real terms %
1990	309,6			
1991	364,5	117,7	135,0	87,2
1992	486,5	133,5	123,0	108,5
1993	583,0	119,8	122,5	98,8
1994	731,8	125,5	118,8	105,7
1995	781,6	106,8	128,2	83,3
1996	892,5	114,2	123,6	92,4
1997	1003,4	112,4	118,3	95,0
1998	1151,3	114,7	114,3	100,3
1999	1476,5	128	110,0	116,4
2000	1651,0	112	109,8	102
2001	1902,4	115	109,2	105
2002	2.286	120,2	105,3	114,1
2003	2.533	110,8	104,7	105,8
2003/1990	-	804	753	107,0

To summarize this part we can say, that Hungarian local government system could be described as decentralisation without subsidiarity. This character causes welfare losses for citizens, as well as lack and waste of resources at the same time.

### 3. Financing of Local Governments

The evolvement of local governments has not only changed the political system, has not only decentralised decision making functions regarding local public services but has also changed the allocation mechanism within the public sector. That shows the new intergovernmental grant system, tax sharing mechanism and the own revenues sources of local governments. The Hungarian local governments' revenues from economic<sup>2</sup> point of view consist of two main parts:

- own revenues,
- revenues allocated and redistributed by central budget.

#### 3.1. Own revenues

##### 3.1.1. Local taxes

Own revenues can be gained from *local taxes*, regulated by a separate law. An illustration of the local taxation system in Hungary can be found in Table 5. Under law, local governments *may* levy taxes that are defined by the law on local taxation, which also defines exemptions and allowances associated with local taxes. The law also includes the maximum tax rates that can be applied. Local governments, at their discretion, can decide whether to levy local taxes of some types or not, and, within the limitations of the law, they can determine the tax rates to use and allowances to grant. Table 6. shows the role and growing importance of local taxes within the revenues. The table shows the importance of business tax which is a type of local tax that is the subject of heavy discussions.

Though in the past decade local tax incomes of local governments have increased substantially in terms of both absolute amount and relative proportion, the local taxation system in Hungary cannot represent a solid basis for local government operations. Nearly 85 percent of local taxes collected in Hungary come from business tax. The basis of business tax is the adjusted turnover of a company or entrepreneur operating in the jurisdiction of a local government. That tax basis is far too mobile, there is no close relationship between the tax paid and the public services used, the principle of equivalency is not observed. That tax basis is rather sensitive to economic boom and inflation, and there is a large opportunity for tax export. That tax basis gives opportunity for adverse tax competitions. From the point of view of local governments service delivery in the Hungarian context the appropriate local tax system consists of three types of taxes, i.e.: a modified business tax, a communal tax and a local property tax. Those taxes would ensure a solid basis of own incomes for local governments.

Competition between communities exists in the case of certain types of local governments in Hungary. The well-known mechanism described by Tibeaut works

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<sup>2</sup> Not regulatory point of view.

partly in the competition between middle-sized or large cities for investors, and between villages for good tax payer residents in Metro areas of large cities. The means used in the competition for investors include granting local tax allowances and/or exemptions, and the offer of serviced land for future production sites. Villages in the Metro areas try and attract residents who want to move out of cities by offering construction land at favourable prices, ensuring thereby that people of high income settle there.

### 3.1.2. Duties and user charges

The following type of own local government revenues are *duties*. There are two groups of duties. The first type shall be paid when property is purchased; the second is due in connection with state administration or court procedures. Their role is not significant, within different statutory constraints, it is cities with county rights and the counties.

Another important element of own revenues is *income from the utilization* of own assets. This type of revenue could be current one, e.g. revenue from leasing municipal assets, premises and plots, yield of securities, etc. The other type of this revenue is the sale of assets. This type of revenue decreases municipal property. The revenues from sales of assets (revenues from privatization) have played an important role in financing local government budget deficit. Table 7. shows the consolidated budget position of the Hungarian local governments.

Table 7.

Year	Local Governments GFS deficit with revenues from privatization (bill. Of HUF)	Local Governments GFS deficit without revenues from privatization (bill. Of HUF)
1994	- 45,5	
1995	8,5	
1996	47,9	
1997	65,2	
1998	- 8,7	
1999	22,9	-122,3
2000	4,9	-108,1
2001	1,2	-91,4
2002	-104,9	-199,5
2003	- 31,6	-40,7

Source: Ministry of Finance

Fee incomes from service provision are less than satisfactory in terms of structure and amount alike.

In association with own revenues, it must be highlighted that local governments in Hungary are entitled to borrow and issue bonds as independent entities. Annual borrowing by local governments are subject to a cap (equal to 70 percent of own revenues minus debt service costs).

Table 5: The Local Tax System in Hungary

<b>TYPE</b>	<b>Charachteristics</b>
<b>Business tax</b>	May be levied on all enterprises, tax base is the net turnover, since 1998 the cost of materials may be deducted, but an increase in the tax rate has compensated for this reduction
<b>Tourism tax</b>	The tax includes rents, guest nights, and summer cottages.
<b>Property tax</b>	May be levied on area size or on the assessed value of privately owned building plots, buildings (flats, houses, garages, cottages etc.) and industrial and commercial property.
<b>Communal tax</b>	Can be levied on household dwellings (owned or rented) and businesses.
<b>Urban land tax</b>	Only on urban land may be levied.

Table 6: Local taxes in Hungary

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
1. Number of local governments levying local taxes	308	1.494	1.518	1.578	1.640	2.297	2.537	2.672	2.813	2.970	3027	3052	3.082
2. Total revenue from local taxes (millió Ft)	9.478	17.221	27.089	33.992	46.383	80.371	111.162	145.826	198.363	221.766	266.685	296.772	322,6
3. Share of local taxes of total revenue (%)	2,5			4,6			9,3		12,7	12,7	13,4	12,8	12,7
4. Weight of different types of local taxes. (Total local tax revenue l = 100)													
- building tax	2	12	8	10	9	10	10	9	8	9	10,6	10,6	
- plot tax	0,2	2	2	2	2	2	2	1	1	1	1	1	
- communal tax of households	3	2	2	2	2	2	2	2	2	2	0,4	0,4	
- communal tax of businesses	7	5	5	4	2	1	1	1	1	1	2	2	
- tourism tax	4	5	3	3	2	2	2	2	2	2	2	1	
- local business tax	26	70	80	80	83	82	84	85	86	85	85	85	84

Source: Ministry of Finance

### 3.2. Revenues allocated ad redistributed by central budget

Under the local government system in Hungary, the central government provides revenues to local governments by sharing central taxes, and providing normative and various targeted grants.

One of the most current and crucial issues is tax sharing. In the Hungarian system the personal income tax is the main subject of tax sharing. The logic of “revenue oriented” financing calls for a significant amount and a stable rule of tax sharing. Table 8. shows that the main characteristic of Hungarian intergovernmental financing is the growing volatility.

Table 8: Sharing of Personal Income Tax (PIT)

Year	Calculated amount of PIT HUF million*	Shared PIT		De jure shared PIT in percentage of total revenues	De facto shared PIT in percentage of total revenues
		HUF million	In percentagen**		
1990	74.530	74.530	100	24,4	24,4
1991	94.038	47.019	50	12,1	12,1
1992	125.972	62.986	50	12,2	12,2
1993	163.177	48.953	30	8,0	8,0
1994	204.327	61.289	30	8,4	8,4
1995	267.517	93.631	(29+6) 35	11,5	9,5
1996	281.317	101.274	(25+11) 36	10,3	7,1
1997	356.979	135.652	(22+16) 38	11,1	6,4
1998	447.725	179.090	(20+20) 40	12,8	6,4
1999	499.660	199.864	(15+25) 40	13,0	4,9
2000	605.785	242.309	(5+35) 40	14,2	1,8
2001	716.340	286.387	(5+35) 40	14,4	1,8
2002	834.895	333.007	(5+35) 40	14,4	1,8
2003	1.012.750	405.499	(10+30) 40	15,7	3,9

Source: Ministry of Finance

\* The actual amount of shared PIT has a two-year lag.

\*\* From 1995 devided the de jure (it is the total number) and the de facto (it is the first number in the brackets) tax sharing.

Normative grants are not earmarked by the state for specific purposes: the important thing is that local governments should be able to provide mandatory services.

Five types of normative calculations are used:

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- Several normatives are fixed amounts for each type of local governments.
  - Some normatives are per capita and have amounts multiplied by population to determine the revenues. Population can be regarded as a proxy for service needs.
  - In many situations the normative amount is calculated by multiplying the number of recipients or beneficiaries of services times the per-beneficiary amount. Essentially all of these normatives are related to education or social welfare, and they give local governments an incentive to deliver some degree of service because the municipalities receive revenues only if there are beneficiaries.
  - One normative is based on the number of beds in homeless shelters.
  - Local tourist tax revenues are matched with Ft 2 each of 1 raised locally.

By expert assumptions the normative grants cover approximately 60 percent of operational costs of obligatory tasks. These grants do not cover the depreciation of assets used for delivery of public services. That means that shared taxes and normative state grants should pay for the services mandated on local governments by laws, but *fail* to finance the total cost of service provision. This fact causes financial imbalances for local governments. This type of imbalance is called in Hungary as the “lack of resources”. It means that all the state regulated revenues do not cover the costs of obligatory services and local governments have no fiscal capacity to match these resources.

In that case the Hungarian regulation uses the deficit grant (ÖNHIKI). This grant is subject of an application process. A series of criteria has been established by law to determine which local government can qualify for deficit grant. These are the following:

- Local governments must levy local taxes.
- Capital expenditures must be less than capital revenues.
- No deposits with duration of three months or more are made.
- The grants are made only to assist municipalities in covering obligatory tasks.

The number of local governments and types of governments has dramatically increased from only a small number to approximately half of all the local governments. Table 9. shows this process which indicates the dysfunctions of the intergovernmental finance system.



Table 9: Deficit grant in the Hungarian Local Government System

	1993	1998	1999	2000	2001	2002	2003
Deficit grant total (bill. of HUF)	0,9	7,7	12,2	12,4	13,6	16,7	15,5
Number of subsidised municipalities	165	994	1362	1169	1208	1423	1238

Source: Ministry of Finance

From the beginning of this financial system, those normative grants have been completed with *targeted grants*, which serve the purpose of implementing investments by local governments, are closed-ended, can be applied for under a local government's own right, and are to finance specific investments. Both types of subsidies reflect the priorities approved by the central government.

Table 10. shows the changes in the components of the revenues of the local governments as well as the changes in the income from the central budget and from their own resources. Table 11.shows the changes of expenditure structure of the Hungarian local government system.

Table 10: Components of the revenues of the Hungarian local governments  
(Unit: percentage)

	1991	1993	1995	1997	1999	2001	2002	2003
Own revenues	18,3	17,3	18,0	23,4	28,8	28,2	27,1	25,4
	2,3	4,4	5,7	9,2	12,9	13,4	12,8	12,4
Shared taxes	11,9	10,4	11,8	12,0	13,3	15,2	15,1	16,8
Capital revenues	1,4	8,0	11,2	15,5	8,9	10,1	9,0	8,2
Normative grants	36,4	34,1	29,0	21,6	18,7	15,3	14,2	14,4
Other intergovernmental transfers	11,6	8,7	9,3	7,6	10,4	10,3	12,6	15,8
Funds received from social security	16,9	14,9	15,6	14,1	13,7	12,6	13,2	14,4
Other funds taken over	1,5	2,3	2,2	4,3	4,0	4,0	3,0	1,3
Debt and other	2,0	4,3	2,9	1,5	2,2	4,3	5,8	3,7
<b>Total</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100</b>

Source: Data from annual reports (Ministry of Finance)

Table 11: Structural components and changes in time of the annual expenditure of local governments

(Unit: percentage)

	1991	1993	1995	1997	1999	2001	2002	2003
Personal allowances	44,1	42,9	43,2	39,6	41,3	41,5	43,3	49,2
from this: employer allowance	12,5	12,2	12,7	12,3	12,6	11,4	11,2	12,3
Material expenditures	33,1	30,9	29,6	27,8	29,2	26,9	25,9	24,7
Expenditure to create reserve from this: own investment	16,8 10,6	17,2 11,7	16,7 10,1	18,0 10,9	18,2 10,4	19,8 12,2	20,8 12,5	16,5 11,9
Subsidies and other expenditure for different puposes	4,7	7,2	8,4	8,7	8,5	8,7	8,2	7,2
<b>GFS expenditure</b>	<b>98,7</b>	<b>98,2</b>	<b>97,9</b>	<b>94,1</b>	<b>97,2</b>	<b>96,9</b>	<b>98,9</b>	<b>98,1</b>
Paying back loans, other expenditures	1,3	1,8	2,1	5,9	2,8	3,1	1,1	1,9
<b>Annual revenues</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100,0</b>	<b>100</b>	<b>100</b>

Source: National Accounts of Hungary and the annual financial reports

Differences in financial capacity between the actors of the local government sector can be experienced along two dimensions. One dimension is represented by *regional disparities*. Regional disparities, which have evolved and increased nationwide, are manifested in the financial capabilities of local governments. They influence the financial opportunities of local governments because there are differences in general economic development levels, employment rates, the characteristics of economic structure, existence of infrastructure, the amounts of personal income tax and the most important local tax (business tax) collected, and utilisation of assets. For example, the personal income tax system in Hungary grants substantial tax exemption to small farmers in agriculture. Now one part of the shared central taxes in the regulatory system on fiscal resources for local governments is personal income tax. That means that the income basis of local governments in communities that are traditionally agricultural ones is less than the actual incomes generated locally.

Regional disparities have further increased differences when the value-based real property taxation system was introduced. By now, however, those differences have mostly been equalised by the regulatory system on fiscal resources for local governments.

The second dimension of financial differences is the difference between various *types of local governments*. Those differences originate from the different fiscal capacities of local governments of various types first, secondly from an uneven distribution of assets, thirdly from the logic behind the regulatory system on fiscal resources.

One of the characteristics of the local government sector is that they possess a substantial part of national assets. The value of local government assets is appraised to be about Ft 3,000 billion. Like fiscal resources, assets are also distributed among local governments of various types and counties extremely unevenly.

From the data presented above one could summarize the main characteristics of the Hungarian local government system. They are the followings:

- one-tire system, the Law on Local Governments regulates all types of local governments. The regulation has avoided a mandatory division of functions between regional level, i.e. counties, and municipalities, i.e. settlement level.
- the structure is highly fragmented, and many small jurisdictions attempt to provide services without desirable economies of scale.
- no obligation by law for small municipalities to cooperate in delivering services. At the same time there are a lot of financial incentives to force the necessary cooperation.

What types of implications come from the basic characteristics of local governments?

- firstly, the expenditure of local governments depends heavily on funding by intergovernmental transfers.
- national policy debate places considerable emphasis on equalization.
- growing role of targeted funding, specific service-related elements in the normative grant calculation.
- growth in the pressure on the deficit and equalization elements within the transfer system.

#### **4. An Evaluation of the Operations of the Local Government System in Hungary**

The operations of the local government system in Hungary will now be analysed along three organising principles. First, it will be explored to what extent the regulatory system on fiscal resources for local governments can meet the constitutional status of local governments and the actual economic situation. Secondly, an overview will be given on the extent to which the solutions chosen can meet the normative principle of fiscal federalism. Thirdly, it will be analysed to what extent the local government system can meet the challenges, mainly the requirements of the accession to the European Union, under its current framework.

##### *1. Constitutional Status versus Macroeconomic Situation.*

Local governments have gained a high level of political independence, which is guaranteed to them by not only the Constitution but also the Act on Local Governments, which is one of the pivotal laws (the amendment of which require a two thirds majority vote by the Parliament), and several Resolutions by the Constitutional Court. However, contradictory to that situation, local governments are too highly dependent on central fiscal transfers, which restricts their autonomy financially. That dependency is manifested in the fact that central government transfers represent a high proportion of the revenues of local governments. Another, equally serious problem is that the regulation on fiscal transfers keeps changing year by year, and there is an increasingly high proportion of central subsidies which has mandated utilization purposes attached to them. That fact decreases the predictability of conditions to the financial management of local governments, thereby increasing

the risks for the sector, thus decreasing their creditworthiness. The improvement of capital absorption capacity of local governments is of *strategic importance*, since by the time of accession to the European Union, the sector's annual net borrowing need may grow to 0.5 percent of GDP (SNDP 1999). Currently, the sector is in a net saving position of 0.6 percent of GDP. Additionally, the net borrowing needs of utility companies in municipal ownership will grow to 2 percent of GDP from 1.4 percent of GDP today.

The above-mentioned contradictions in the intergovernmental financial regulatory system stem from general economic problems of transition. In addition to the effects of the transformation crisis, the regulatory system on fiscal resources have soon been faced with the dilemma of providing incentives for generating incomes, maintaining interest in independent financial management, and equalising territorial disparities. Due to understandable reasons, the system of financial regulations has moved towards *equalization*, which reduced the relevance of the principles originally declared. Equalisation had to be introduced, as a correction, in the regulatory system on fiscal resources not only due to rapidly spreading regional economic disparities. The application of the regulation on local governments' fiscal resources has also caused disparities between the various types of local government, the correction of which has deformed the system.

Due to its logic, the subsidization by the state of investments implemented by local governments is "out of place" among normative grants. The majority of transfers are in the form of targeted grants, which means that the central government has an important role in defining development priorities. Such targeted and addressed grants, which reflect central priorities, help the implementation of an estimated 60 percent of the investments of local governments. Even a fine-tuning that has been carried out on the addressed grant system cannot help with its problems. A significant sign is that the amount of addressed transfers granted but unused has increased year by year. Additional problems have originated from the fact that the system of state transfers for investments is of *multi-channel financing*. First, the multi-channel financing means that in theory a project may be financed from several fiscal sources (e.g.: targeted grant, decentralised state subsidy of targeted-type). Secondly, it also means that in some cases the transfers, which cover operating costs and capital investments, are defined in different subsystems of the general government, e.g. the operating expenditures in health care are financed by the National Health Insurance Fund, whereas the funds for capital investments, some of which have got associated future operating expenses as well, implemented by local governments in the health sector have to be arranged for by local governments from some of their own incomes, state subsidies, and perhaps borrowing. It is clear that in such situation, health care institutes have many times built superfluous capacities, and have to face situations when they lack funds for operating expenditures, or are insolvent.

Last but not least, the regulatory system of fiscal resources has not been prepared to tolerate an increase in assets owned by local governments, and the effects thereof. A

local government's assets position has a contradictory effect on the owner's fiscal position. The two extremes of possible effects are the following: the utilisation, i.e. leasing or selling, of an asset, which is marketable and can be used for non-governmental purposes, will increase own incomes. The maintenance or rehabilitation of an asset transferred for the purpose of mandatory service provision will represent a large expenditure item. Local governments with substantial marketable assets have financed the deficit of their operating budgets from the sale of those assets, leading to loss of assets for many of them.

Those processes are duly reflected by the changes in the budgetary structure of local governments. The own incomes of local governments represent an increasing proportion, normative and other subsidies represent a decreasing proportion. Among own revenues, the local tax income shows the largest increase. Revenues of local governments from privatisation are also high. However, this latter item cannot be expected to grow in future due to a decrease in the, so-called, shared privatisation incomes (coming from privatisation by the state). It is important to note that both the local tax basis and incomes from the sale of municipal assets are distributed very unevenly among local governments of various types. In the local government sector in Hungary, 200 local governments possess 80 percent of local tax incomes, and 70 percent of the assets recorded. As a consequence, under the current local government structure (many local governments of many types), the aim to give incentive to local governments to generate income, as it is included in the regulatory system on fiscal resources, is achieved in the case of a small proportion of the governments only.

Paradoxically, the lack of economic conditions to autonomy goes hand in hand with a dissatisfactory quality in financial management in the sector. That situation can be explained by the lack of appropriate expertise, and the lack of external and internal financial control of the sector.

## 2. *Municipal Finances as Compared with the Theory of Economics*

There is an extensive professional literature available on the topic of municipal finances (NETZER-DRENNAN 1997., MUSGRAVE- MUSGRAVE 1989 and BLANKART- BORCK 2000). The literature tends to provide the following argument for the decentralisation of fiscal functions: the applicability of local public goods, efficiency in allocation, competition between communities and utility principle of taxation. Now that logic will be used to provide an evaluation of the system in Hungary.

Local public goods are used to refer to those goods, which have the characteristics of public goods, but are consumed by a relatively small local community, e.g. public lighting. Another type of ideal for public goods can be interpreted on the level of the central state, e.g. national defence. The goods and services provided by the state and/or local governments substantially differ from the ideal type. That means that first, no optimum arena for the provision of those goods can be defined; secondly, some of those goods are not pure public goods but either fee-paying goods or club

goods. At the birth of the local government system in Hungary, it was not clear to what extent the formerly developed system of service provision by the state has to be dismantled. In that situation, decentralisation was also a means of narrowing the circle of public services. Thus the distribution of tasks between the central government and local governments was subject not only to aspects of finances and economic viability, but also party politics.

The considerations associated with efficiency in allocation could not be enforced in an undisturbed fashion. The structure that evolved was extremely fragmented. Table 2 shows the sizes of local governments in some EU countries and in Hungary. The fragmented nature of the system in Hungary goes together with a list of mandatory services that is long even in international comparison. This peculiar “Hungarian model” cannot meet the elementary requirements of economies of scale and quality. Thus the low efficiency of the sector represents an obstacle to the competitiveness of economy in general. Enforcing efficiency in allocation is a substantial challenge in the further development of the system.

### **5. Challenges and Possible Aims of Reform**

In relation to financial management, local governments have to face two major challenges. First, local societies demand an increase in the quantity and, more importantly, *quality* of public services i.e. environment protection, urban and suburban mass transport, healthcare, basic education and trainings. Secondly, the ability of local governments for absorption of funds will primarily decide whether the *short- and middle-term benefits* coming from the European Union membership can be realised or not. The basic original structure and rules are rational. To meet the need of improvement the regional competitiveness and the absorption capacity of the Hungarian economy, the main objectives of a *possible* local government reform are the followings:

- to increase the quality public services delivered by local governments, to force the effectiveness, efficiency and economy of providing collective goods.
- to strengthen the fiscal capacity with the introduction of a new tax sharing system and new types of local taxes.
- to reduce the volatility and increase the transparency of the intergovernmental grant system.
- to increase local accountability.

Whether those challenges can be met will depend on the conditions on *macro-, mezo-, and micro-levels*.

### **5.1. Macro aspects**

By macro conditions I mean the laws governing the operations of the local government system. In other words, laws to stipulate units of public administration, electoral districts, the definitions of the various levels of local government and the competences of those levels, how to levy and collect various taxes and the operations of NGO's. Macro conditions also include *legal security* associated with the operations of the sector, and the state's priorities of economic policy, which are manifested mainly in the fiscal policy. The situation in Hungary in the past was characterised by a contradiction between legal regulations and the priorities of economic policy. Those contradictions were related to the fact, among others, that the Act on Local Governments provides the financial management of local governments with an autonomy that is unparalleled even in European comparison. Some of those rights and some irregularities that were against the intentions of legislators even, e.g. the option of unlimited indebtedness, have been amended meanwhile. An important loophole in regulations has been eliminated by the adoption of the law on local governments' debt settling procedures. However, it should be understood that some of those solutions were based on short-term priorities of economic policy, and thus require further amendments.

### **5.2. Mezo level**

By the mezo level I mean the general rules of game to the state's financial management and the regulatory system on fiscal resources for local governments. Under the decentralisation process of public services, the central government allocates some of the state incomes necessary for decentralised services, and provides funds for the equalisation of disparities stemming from economic development. The operations of local governments is highly influenced by the techniques used within the general government for planning those processes and for allocating funds, and the control mechanisms and subsequent verification opportunities that are available for ensuring a necessary feedback. Regarding the system currently in operation, it can be stated for certain that it requires an overall reengineering, and some parts of it, i.e. the system of targeted grants for investments, require radical transformation. The application of the regulatory system on fiscal resources requires far too high transaction costs to be paid; the functions of service allocation and equalisation are mingled; control mechanisms are used exclusively on the rightful utilisation of fiscal resources; and there is a want of criteria of expediency, efficiency, and effectiveness (VEREBÉLYI 2000).

### **5.3. Micro level**

By the micro level I mean the internal way of operations and financial management culture of local governments and their institutions, organisations and non-profit organisations, which are all determined by the two above mentioned levels. Those two items include the way service provision is organised; the organisational framework used for service provision and financial management; the cooperation developed by

local governments with other local governments, the competitive sector, and with the money- and capital markets; and transparency on financial management.

## **6. The Directions to and Possible Scenarios for the Further Development of the Local Government System in Hungary**

Further developing macro conditions basically means creating the legal conditions to change the system, which is fragmented and, therefore, not efficient. Several positive scenarios can be conceived in that area.

### **6.1. First Scenario**

Under *the first scenario*, the political conditions necessary for the change (two thirds majority approval in the Parliament) will not be achieved. Then the central government may decide on giving further incentives, stronger than earlier ones, for creating local government partnerships. That would mean that, *in lieu of* the current investment transfer system i.e. targeted grants granted to some of the applying local governments submitting proposals, state transfers would be given to facilitate the process that various fundamental local government services, e.g.: primary education, social care, are provided under local government partnerships. That solution may go together with a reform in the tax system in Hungary, which would strengthen the income basis of local governments. Additionally, it would be possible to adopt some institutions and legal regulations to ensure creditworthiness and financial transparency for the sector, e.g.: creating a state credit guarantee fund for local governments. *The implementation of those measures that the previous sentence contains would also be necessary in other scenarios as well.* In my view, the centralisation of the financing of the local government sector under the French model is a less desired but possible option.

### **Second Scenario**

The second scenario includes the amendment of the pivotal Local Government Act. The amendment would provide an opportunity for the transformation of the distribution of services between the state and local governments, and the organisation framework and/or financing system thereof. Under this scenario too, it is possible to carry out a tax reform and create the regulatory elements and/or institutions to facilitate the improvement of financial transparency and creditworthiness. Based on some on-going efforts it seems that two possible options are available within this scenario.

One option, the chances of which I consider higher, can be a transformation of the local government system, in which the “basic unit of financial management” is the city and its Metro area. This “district-based model”, which is well known in a number of European countries, would make service provision by local governments far more streamlined. That model would substantially reduce the number of actors making actual financial decisions (to a few hundred down from over three thousand at present).



The second option means the development of a regional middle-level with independent political legitimacy, financial funds, and income basis. That solution can attain its purpose together with the transformation of the tax system in Hungary only. Using the categories of the European Union, the strengthening of NUTS II and NUTS III levels may represent an effective solution not only from the perspective of increased absorption capabilities of development funds from the European Union, but also from the perspective of better handling the disparities, which have widened as a result of the change of regime, and from the perspective of the neglected complex regional development system. Table 1 shows the Hungarian public administration system under the NUTS.

The implications of the above scenarios on the mezo and macro levels are the following:

- On the mezo level, it is absolutely necessary to carry out a state accounting reform to cover the financial management of general government as a whole, to introduce accrual-based accounting in addition to the existing cash-flow-based accounting, in order to ensure the conditions for replacement of fixed assets (accounting for depreciation). Additionally, preliminary control institution and mechanisms should be developed for the sector, and external auditing should be arranged for in a satisfactory manner. That should be based on an appropriate cooperation between the State Audit Office, the Government, and private auditors.
- On the micro level, the financial management culture should substantially be improved. Preconditions to it include ensuring appropriate expertise, developing controlling systems, and developing an internal control system to enable legal, regular and effective operations.

## **Conclusion**

Hungary, along with 9 other countries, has been a full member of the European Union since May 2004. The enlargement will create a new situation within the EU as well. The cut-throat competition for the subsidies of the Union can already be seen. In this competition the Hungarian economy will be able to succeed only if its local government sector operates efficiently, possesses own income, functions transparently and the local authorities take the responsibility of economising. So the stake of the reforms is not negligible.

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**BEHAVIOURAL APPROACH OF MANAGEMENT SCIENCE  
- FROM THE ORIGINAL IDEA TO THE CONCLUSIONS -**

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'The wise man lives in accordance with the nature'

Lao-ce

I have had an affection for the nature since my childhood. I have felt attracted by the discovery of the tiniest details, quivers as well as by the interaction of complex, embedded systems.

It is my firm belief that human versatility and sensitivity to the things of the world around us are to the advantage of both the individual and the society.

Complexity of human behaviour and the desire to acquire this knowledge have committed me to do scientific research of human character and the relations of human groups.

What can be the secret behind the unrivalled success of Homo sapiens, the intelligent man? What is the driving force behind his deeds? How could we explain the behaviour of human race and that of ourselves? Questions like these have engaged the attention of mankind for a long time.

Several disciplines like philosophy, psychology, anthropology and sociology have tried to answer these questions in different ways. Despite all the efforts there are still blank spots, there is an increasing demand for synthesizing the isolated results.

Collecting the answer pieces we have to take into consideration the natural scientific results producing resounding success in behaviourism. Ethology, evolution biology and genetics have surprised the world with inventions that are welcomed by scientists of other fields as well.

Before starting my research work I wondered what kind of results can be expected from collective examination of human ethologic attitude to behaviourism, human factors of management science and management psychology and whether these results can be used in organisational circumstances. I come to the conclusion that the scientific results of human ethology explaining human nature and behaviour originating from evolutionary roots can be employed profitably in management science as well.

That was my original idea I built the brand new approach on.

With authentic knowledge of human character and driving forces of our behaviour and applying this knowledge to organizational circumstances in the workplace we can increase both the individual and team achievement. Besides we can also form working conditions better adjusted to our nature and genetical inheritance and through this, our job satisfaction can be improved significantly. It is the category of joy that can be shared by the superior and the subordinate alike.

With my dissertation on the one hand I would like to contribute to the synthesis of so far accumulated knowledge of different disciplines, on the other hand I intend to restore the lost balance which made the behaviourists in the past examine mainly the differences caused by local customs and traditions.

I believe that emphasizing the differences existing on the surface can sometimes overshadow the deeply rooted and very significant similarities. These similarities are of great importance in exploration of human behaviour.

My research investigates peculiarities of human nature based on genetical inheritance in the workplace hoping to discover appreciable factors from the point of view of management science. My work focuses on an interdisciplinary field, that requires sociological and scientific knowledge and methods as well. In my opinion, in spite of this twoness, investigation of Management Science in the mirror of Human Ethology rest on rational basis. Nowadays we better and better show interest in scientific research of human nature, behavior and society. We would like to find scientific answers to our problems related to our family, place of work and other communities.

I think that by way of introduction I have to say some words about Human Ethology. Ethology deals with the behavior of animals, while Human Ethology deals with the behavior of humans. Human Ethology is an evolutionary science. It takes it that learning, tradition and culture play an important role in human behavior, but the capability for culture is a result of an evolutionary process. Structures and dynamics of possible cultures are formed within the limits of genetic. Human Ethology takes the culture as a behavioral system with keep in view that components of culture are formed in learning activities, but as behavioral patterns they are suitable for ethological and evolutionary analysis. Analysis of species-specific, inherited behavioral patterns is one of the main task of Ethology and Human Ethology. The first reflections on Human Ethology was published by Konrad Lorenz, founder of Ethology. Ethology certainly found its way. The basic concepts stood up against challenge. As is usual in a fast developing discipline, focal points of interests shift. The evolutionary approach certainly continues to attract the attention of the other disciplines of human behavior. Human Ethology also profits from the numerous sociobiological contributors. Two international journals - Ethology and Sociobiology and Human Nature - publish regularly contributions, and the Human Ethology Newsletter is developing an important discussion format. There are however also matters of concern as regards methodology.

Konrad Lorenz emphasized again and again the importance of observation and description, but over the years we can observe a trend away from original observational data. William Charlesworth documented this in a recently published investigation in which he analysed. There is a clear trend away from empirical papers toward theoretical ones. Another point of concern is a "nothing-but-an-animal" presentation of the human being. When Desmond Morris started to characterize the human being as a "naked ape", it was meant to put the fact of our phylogenetic history into the focus of attention. It was meant to shock as a didactic measure, and as such was appropriate at that time. But if one were to conclude that such is the complete way biologists see the human being, one would be basically wrong. Konrad Lorenz emphasized repeatedly that no one is able to appreciate the uniqueness of the specific human attributes as clearly as those who can perceive them against the background of the much more primitive actions and reactions, which we also share with the higher animals. Reason and the morality based upon it, the capacity to learn a language and to talk about present, past and future events, to pass on knowledge and thus to build up culture, and finally, our ability to set goals for ourselves on the basis of desires and

empathy are indeed unique. And this provides us with new potentialities for survival as will be discussed at the end of this contribution.

In spite of this emphasis on the uniqueness of human nature, many biologists perpetuate this nothing-but-an-animal presentation, often by means of appalling illustrations depicting grimacing monkey and human faces, the message being that they are "all the same". This is not just a matter of taste, but harmful to our field since we need to communicate and cooperate more than ever with the humanities. Without understanding culture, we cannot understand the human being who is "naturally cultured". Humans are certainly outfitted with motivations, emotions, biases in perception and with innate motor patterns given as biological heritage. And part of this heritage we share with animals. However, as an old Chinese proverb states, all that is animal is in humans, but not all that is human is in animals.

What are the prospects of Human Ethology? The investigation of our phylogenetic heritage programming our action and biasing our perception and cognition is still a tremendous task ahead of us. In particular the universal grammar of human social conduct, verbal and nonverbal alike, needs further exploration. Man is a cultural being by nature. He is genetically endowed with the capacity to acquire a language and speak, which allows him to tell others what to do and when, without the need to act as a model. Cumulative culture as a result has made human history a story of success. We have amongst others, however, created ourselves an environment which deviates from that which exerted its shaping influence through selection for most of our ancestral history and this confronts us with some problems. Our ancestors lived in small face-to-face communities with a simple technology, foraging as hunters and gatherers. Modern man lives in anonymous million societies, in urban environments outfitted with the means of technical civilisation. All in all, the development has to be considered as progress, since without societies of millions there were no universities, no large libraries, no concerts or opera houses, and no technical civilization with all the new options including the conquest of distance and space. Within our century, we proceeded from the first clumsy automobiles to space travel, from the mechanical age to the electronic age. We can hardly imagine what a species achieving this in such a short of time could achieve in another ten thousand or more years, if it were to solve its social and ecological problems.

Overpopulation and environmental destruction threaten the very basis of subsistence for future generations. We certainly need a new generation encompassing a survival ethos, carried by a feeling for moral responsibility for future generations. There are however in our phylogenetic heritage dispositions which we have to face, which in our present situation hamper the very development of such an ethos. One is our being programmed for the sprint in the present. Ever since the first creatures of our planet competed for scarce resources, what alone counted was to win right now. This selected for opportunistic exploitation to the maximum of any opportunity. This was also of advantage to our ancestors until fairly recently. And we are well equipped for this type of competitiveness, since we use our strong aggressive dominance striving instrumentally in many ways, not just in the social context, but also to overcome any obstacles. We sink our teeth into problems, we attack them and subdue nature. This together with the fixation on the present seriously hampers the development of an ethos which takes into consideration the fate of future generations.

This trap of short-term thinking has to be avoided. In order to achieve self control, we need to learn about those traits which in certain situations of modern life prove maladaptive, and others which we can tap in order to adapt anew.

We need to learn about the range of modifiability for each of our behavioral characteristics. We must know about innate learning dispositions such as our indoctrinability, be they helpful or maladaptive, and if so in what situations. History and the study of the cultural manifestations of man in historical and prehistorical time provide a wealth of experiments to be studied.

Based on my original idea I investigate Management Science in the mirror of Human Ethology. In this case, approaches focusing on human sociality, cooperation and team work have great significance. I elaborated a complex research methodology with a combination of methods used in natural and social sciences. As a result, during my investigations I applied questionnaires, interviews and hidden or undisguised observations. I chose samples from two different types of organisations. On the one hand it was an educational institute, University of Miskolc, and on the other hand a very competitive company from the business sector called "KFKI", as one of the leading Hungarian IT Holding Co..

During my research work I systematized the previously examined sub-fields in Ethology. I studied whether these topics are suitable for investigation from the viewpoint of Management Science as well. As a result of this "double-checking" method, three main fields and six sub-fields have been outlined:

1. Connections
  - 1.1. Contacts
  - 1.2. Typical Connections
2. Groups
  - 2.1. Group-structure
  - 2.2. Synchronization
3. Dominance
  - 3.1. Aggression
  - 3.2. Dominance-alternation

The fields mentioned above are the objectives of my deep study. I do not give here full details of sub-fields to be investigated, because firstly I would like to focus on the Conception of Research. So, the second step was a revealing investigation. In this phase I tried to find out, that concrete behavioral patterns, successfully explored before in Ethology, whether exist in human organizations or not. If the answer yes, the next question is when, in what kind of situation and which way they are present. These results were the basics of further research. Deep investigations revealed conclusions, that could be successfully applied in Management Science, for instance creating a team or a company structure, decreasing of aggression between the colleagues, elaborating a friendly, harmonic environment and so on.

To sum up my general conception I hope that concrete results of this research have some significance beyond conclusions can be drawn from separate investigation of Human Ethology and Management Science.

In my opinion a detailed research of these factors in institutional forms can provide new, forward-looking information, results and methods, social significance of which cannot be neglected.

Let us take a closer look at the main results step by step.

Based on the previously executed Human Ethological examinations and my research we can conclude that evolutionary components of human contact forms unambiguously can be revealed even in organisational circumstances. The social attraction, that is the main common feature of human and primates, we can handle as one of the most important characteristic of our day-to-day organisational behaviour. "The man is a social animal" phrase was totally confirmed in organisational atmosphere as well. Positive human feelings supported by various types of contact forms can effectively stimulate both working performance and general state of health. Knowing psychological effects of these, in my opinion is a managerial responsibility. Similarly we must ensure possibilities of these contacts, that can represent such a "power" can not be neglected by anybody who feels even such a low responsibility for his organisation.

Within my first research group called "Connections" I revealed typical working connections between males, moreover leading role of them was also confirmed. To reveal the casual system of this evolution based feature I had to extend my investigations to free-time activities and social environment of the sample as well.

Behavioural patterns and features originated from sex differences have enough importance to take them into consideration in our everyday life.

Nowadays we often emphasize a modern leading style that strives for harmony with preferred human relations. In such an environment we can usefully implement knowledge coming from phylogenetic view of investigation of gender differences. Getting acquainted with our employees' behaviour and personality is essential to become a good leader including the above mentioned genetic features too.

Having investigated group-structures from Human Ethological point of view I can state that all of the generally existing group-intervals can be detected among employees' informal relations. Nevertheless formal groups within an organisation are often show different picture. In my opinion if we find such a difference, that is the best to turn my theory into practice. First steps we have already taken in the real life at "KFKI" are very promising. Forming groups based on our genetic heritage can result more efficient and better organisational atmosphere at the same time. Naturally there is no one absolute scheme that we can fit all situation, given intervals are just for approximate solutions, besides we have to take into consideration the type of activity as well.

Synchronizational processes played important role from the early stage of human evolution. Similarly not a single could exist and develop without behavioural synchronization. There are many types of it, from a simple smile to very complex, often unconscious actions. All of our common goal is to ensure primary conditions of the highest possible organisational synchronization.

After a detailed examination of various types of aggressive behaviour it became clear that there are easily distinguishable categories we can make based on observations and interviews. Human aggressivity even in organisational circumstances exists on a day-to-day basis. Its type of appearance and strength may vary depending on lot of conditions. They can be gentle and hardly detectable, but sometimes they also can lead to violent conflicts. Handling these personal or group conflicts occasionally can have great importance. To be better and quicker human problem solvers it is high time to learn more about psychological and ethological aspects of our nature including knowledge of aggressivity too.

I found that in organisational circumstances control-mechanisms derive from abstract forms of aggression rule informal hierarchy and dominance structure. Biological disposition makes existence and development of dynamic and parallelly differentiated rank order possible. It has been verified that we, who work collective highly accept our position in hierarchy we are put, but we make efforts to get higher and higher on the social ladder at the same time.

My investigations aimed to reveal personality features of a good leader from the phylogenetic point of view stated that two things are very important. Without continuous professional self-improvement and taking care of human relations we probably never can be successful leaders.

Order refusing capability of man is an extremely weak developed characteristic of us. We rarely and hardly refuse directly our bosses' order. It is because of the common feature of obedience and submissiveness of our species can be connected to high rule adoption capability even in organisational circumstances.

From this pile of results discovered by the research all people working in organized conditions can profit, regardless of the place they occupy in social hierarchy. Man is a 'social animal' and it is valid for each of us despite the differences originating from personal characteristics.

Not a person working in community can get rid of the consequences arising from this fact, so the exploration of that is essential for the employers and employees as well. From the answers employers gave to a questionnaire turns out clearly that paying attention to their subordinates, solving their problems comfortingly are of great importance for the leaders. The findings of my research exploring the characteristics of human nature in the workplace can be utilized in situations like calming aggression, creating synchrony, forming the ideal team for a task or strengthening human relationships etc.

I think the results of different research fields can be employed profitably in practice as 'influencing zones' where a problem connected with management psychology, reorganization or conflict management can occur. I can provide help to the solution of such problems on the basis of my behavioural research. Taking these findings into consideration can result in a more effective and pleasant atmosphere in team work and in organisations.

Let me remark that this knowledge can be beneficial from another point of view as well. In our rapidly changing world discoveries that are constant and valid in the long run can be considered rarities. But genetic components effecting human nature



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besides environmental factors can be regarded as permanent because of the slow and conservative nature of evolution. So the effects of genetic factors influencing our colleagues' behaviour will be verifiable in the following generations too.

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## **GENETIC ALGORITHMS IN ENVIRONMENTAL ECONOMICS MODELLING**

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### **1. Introduction**

The idea of applying biological analysis in economics is not completely new. In the 19<sup>th</sup> century Alfred Marschall (1890) considered economics to be a branch of biology. Others, on the contrary, looked at biology as one of the branches of economics (Mohr, 1990: 209-219).

The most widely used form of relationship research is looking for identifying analogues. After conducting an analysis of the two, it can be stated that the processes of functional and evolutionary biology are similar to some extent to those going on in economics. The similarities reflected in the processes provide a basis for the interdisciplinary development of economic ideas and modeling, which can be the precondition for new scientific findings. Thus, it can be concluded that there is a great need for a similar change in the approaches of environmental economics as well.

One of the aspects of interpretation of modern environmental economics is a scientific and within this a biological approach. The basic method of looking for the ways of establishing relationships between branches of science is looking for analogues. Finding similarities is the first step towards realizing what roles and functions the analogues play in scientific research. The examples listed and introduced in this study show that there are analogues that can be applied in the fields of economics and functional biology, as well as evolutionary biology. The basic objects and processes bear general similarities, however, their degree differs.

The flora and fauna of the present time has developed in the process of biological evolution. Biological evolution is still going on: it is a dynamic process. Since it has a time horizon exceeding the human pace, a superficial observer can hardly notice its development and changes. This process started with the evolution of molecules about 3.5-4 billion years ago.

Examining the common analogues of biology and economics, three types of analogues can be distinguished (Birner 1996:30; Knogge & Knogge 2000:2-3):

1. Spotting similar theoretical controversies in both branches of science.
2. Application of biological arguments in confirmation of economic hypotheses.
3. Looking for conceptual analogues and their application in both disciplines.

## **2. Characteristic Features Of Integrated Environmental Economics Operating On The Basis Of Genetic Algorithms**

Genetic algorithms are derived on the basis of Darwin-type biological evolution and the process starts from a possible state (population), in most cases chosen at random. New generations emerge from this starting generation on the basis of various procedures. These generating procedures go on until the best solution to the problem is found. Selection, recombination and mutation are the most important genetic procedures. During selection the algorithm applying genetic procedures selects the parents giving birth to offspring. The individuals of the current population are selected on the basis of their fitness value and with defined opportunities. The fitness value shows the appropriateness of the individual applying the fitness function. While producing offspring recombination changes certain parts of the parents' chromosomes in a similar way as natural genetic recombination. During the process of mutation several parts of the chromosomes start changing at random.

As can be seen, drawing a parallel between biological and economic evolution provides an opportunity for the description of dynamic economic processes changing in time by using genetic algorithms. The first step in finding algorithms in biological and economic processes is to draw a parallel between the terms used in both disciplines and to determine the degree of elaboration of analogues. On the basis of these ideas it can be stated that most biological terms can be used both in economics and in the social field, which satisfies the essential condition for successful modeling.

Since 1990 numerous articles on the application and applicability of genetic algorithms used for the description of economic processes have been published and much research has been carried out in this field. Arifovic (1994) and Dawid (1997) applied algorithms for modeling of Cobweb-type markets and for the evaluation of trends in production and profit development. Brenner (1998) examined whether evolutionary algorithms could be applied in the description of study processes. Birchenhall (1995) used algorithms for modeling technological changes. Birchenhall (1997) analyzed the Cobb-Douglas-type production function. Lawrenz (1999) was interested in whether using genetic algorithms to analyze the security market could achieve as rational results as ordinary methods of analysis. Arifovic (1998) modeled the development of the rate of exchange in two trading countries. Reichmann (1999) evaluated the stability of economic behavior by using genetic algorithms.

### ***2.1. The Structure Of The Model***

The model operates on the basis of basic genetic operators (selection, recombination and mutation). The specific aim of the algorithm under specific circumstances is to minimize the pollution caused by a company. The level of pollution (if there is a possibility to develop a new strategy) has to be defined by the application of an objective function from generation to generation. (In the figure this step is

shown by the evaluation of the starting population). If the target level for the pollutant emissions is not met, the genetic procedures come into force. (Figure 1)

The individuals of the new generation develop in the process of the genetic algorithm. The first step is the selection step, when the strategies are selected on the basis of their suitability. The degree of the strategy of (individual) suitability determines its sustainability possibilities. This sustainability can be determined by the fitness function. While determining the fitness function all the elements of the complex company objective systems have to be taken into account. The new strategies emerge in the process of recombination. Then, during conscious mutation or mutation chosen at random (as has already been mentioned both can appear in the operation of a company) the final strategy variations are developed. These variations have to be examined in order to elaborate modeling very similar to the real situation and to determine whether the variations meet the real expectations and can be implemented in the current situation. It can happen that during recombination and mutation unrealistic strategy possibilities can be developed and have to be eliminated from future processes.

After this the strategy is again evaluated with the help of the objective function. If the target level for pollutants is met, the process is over. If not, it is reiterated until our system meets the interruption requirements.

Mapping of all the types of relevant company behaviors provides a basis for the determination of the starting population. The sphere of behaviors is defined by the internal and external factors of company operation. Internal factors include current and potential production technologies, as well as the available amount of human and real capital. Figure 2 shows the system of relationships between environment-based company factors and external factors as well as the definition of the environmental tolerance to be fit into particular strategies.

The environmental tolerance can be determined at company and total market levels with the help of one-population or multi-population algorithms. In both cases the basic objective is to create an effective model for the environment tolerance taking into account the current conditions. In the case of modeling done by genetic algorithms the genetic procedures (selection, recombination and mutation) can be applied to the analysis of one or several companies.

In case of a one-population model under the individuals of the genetic algorithm we mean possibilities and strategies of the environment-based company behavior that can be exhibited in constantly changing macro and microenvironments. The whole population is made up of its complexity. As for the multi-population model there are two parallel running genetic algorithms. In the first each environment-based company strategy used by companies is created on the basis of algorithms applied at a company level, as well as the environment tolerance constituting the starting population of the algorithm running at a higher level. The second parallel algorithm is used for measuring the total pollution emitted by all the companies.

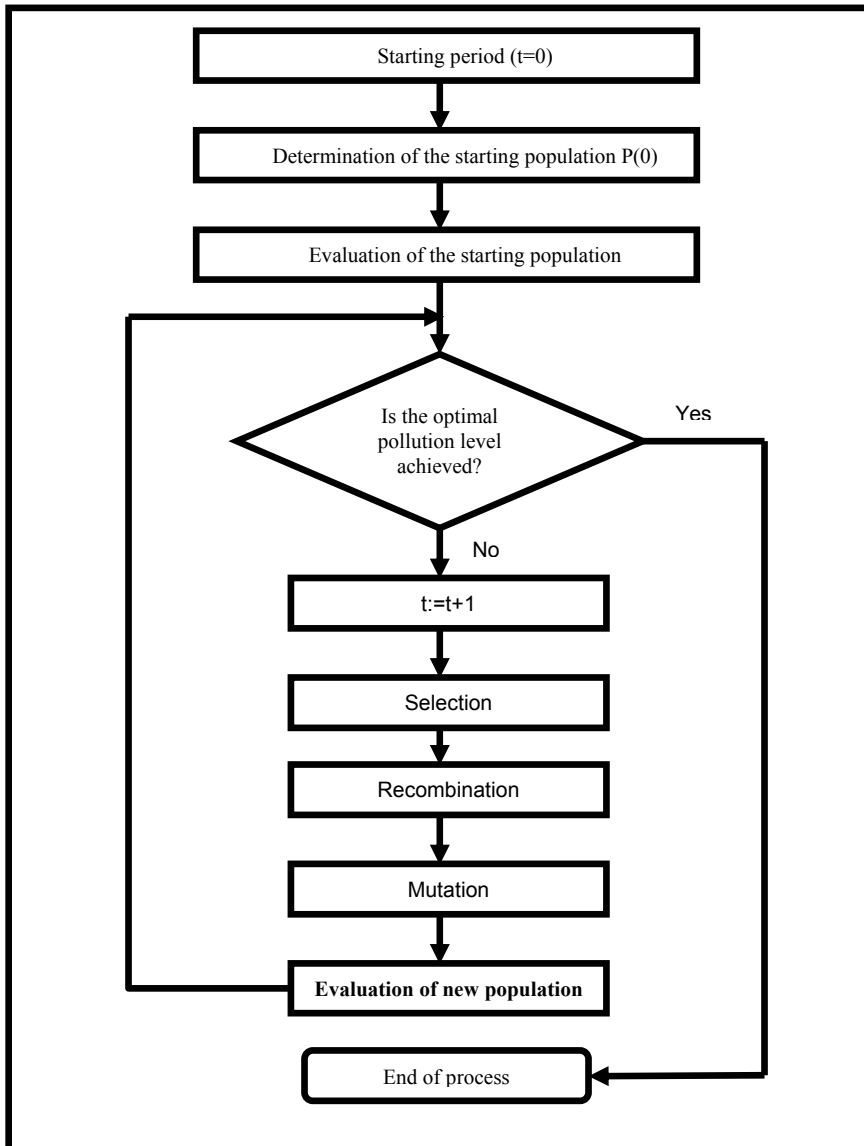


Figure 1: Environment-based market modeling applying a genetic algorithm

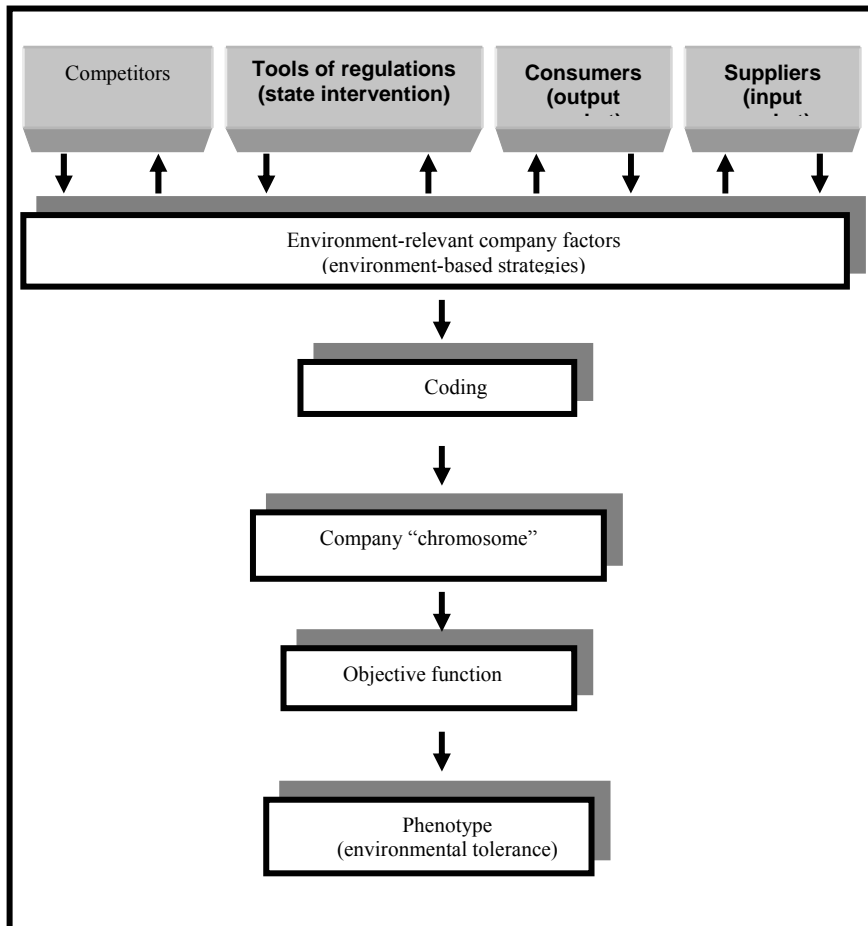


Figure 2: Definition of the starting population

The first step of genetic algorithms taken in a less broad sense is to represent the obtained information, that is to code the chromosomes. While elaborating the code the synchronization of different units of measurements has to be taken into account. If for their analysis the existence or non-existence of only one factor is needed as input, the yes/no, that is the 1/0 is needed in the case of binary coding. However, if quantitative coding is required, that is the Gray-code is used

The Hamming-deviation ( $D$ ) was used to compare the methods of coding. It shows the amount of numbers to be changed in order to obtain one binary code from another. For the Gray-code this value is even, but it is changing in the traditional binary code. Thus, in the mutation at random (not an exact imitation of somebody else's strategy or the lack of exact information) the torsion is lower, but in directed mutation (conscious technological change) the expected results may not be obtained. So the application of the Gray coding system may have advantages and disadvantages

in modeling. It can be stated that the most accurate coding can be achieved by choosing the method by the factor. As a result a profound knowledge of gene boundaries and their mapping is of utmost importance. The position of a particular gene is to be accurately spotted, otherwise, false results will be obtained in further procedures.

In the models offered by Arifovic (1994) and Birchenhall (1995) no difference was made between the objective and the fitness functions. We might not be right when assuming that the basic and the only objective of the company to be modeled is the reduction of the burden on the environment. It could be considered to be the only objective if the other elements of the company suffer no harm. Formulating this idea more precisely, it means if compatibility, the target of maximum profit in the long run, productivity and other factors were not neglected, if they were constant, perhaps pollution could be reduced. However, this cannot be achieved without bringing about changes in the external conditions. It is obvious that this condition would considerably limit the circle of strategies to be applied. Several strategic factors have some impact on the pollution. As a consequence of this the function formulating the only objective has to consider several factors (current elements of the strategy) to be an input.

Since our model is very unique, in case of genetic algorithms a difference should be made between the chances of proliferation of an individual and his successful outcome. In the genetic algorithm the objective function measures the success of a particular individual regarding the objective to be optimized, whereas the fitness function evaluates the chances of proliferation of an individual. As our model targets the definition of the level of pollution, the objective function determines the strategy depending on the amount of the emitted pollutants and by using the terminology of the genetic algorithms it defines the phenotype of the genotype. On the basis of the factors of the company objective function the fitness function represents the biotic potential of the company strategy and of the production technology reflected in the model. A multifactor company objective function determines one of the elements of company decisions, namely the strategy.

It can be concluded that there is a difference between the objective and the fitness functions, because in real life a company does not take decisions focusing only on one dominant objective, as it has a system of complex objectives. Furthermore, partners having business relations with the company (on the market and outside it) do not always manage to reduce the burden on the environment, as a result of which the issue of environmental protection does play a central role in the objective system of the company. That is the reason why the success and the biotic potential of the company strategy – determined on the basis of the objective function – are separated.



## 2.2. The Selektion

In the order of genetic algorithms the first genetic operation is selection, in the process of which the algorithm selects the parents, and the descendents originate from using genetic procedures.

*In our model selection is a specific selection process, which chooses the most suitable environment-based company strategy to be used in the future, taking into consideration its suitability for definite conditions and applying external and internal factors of the company.*

The most common and widespread selection algorithm is the so-called roulette method. It is similar to a lottery wheel divided into several parts. The width of the pie slice is in direct proportion to the selection probability of the individual belonging to it. The wheel is turned  $n$  times and parents of the next generation are selected. It is obvious that the higher fitness value an individual has, the better chances he has of being selected several times. Thus, there is a risk that all the selected individuals will be identical. Although this method has a relatively high deviation between the target and actual selections, it is the most widely used one. The deviation is much lower in the case of stochastic sampling. Let us take the lottery wheel again to illustrate the idea. The width of the pie slice is also in direct proportion to the selection probability, but in this case the  $n$  numbers are placed around the wheel ( $n$  represents the number of individuals). The wheel is turned only once. The individual is selected for recombination as many times as the number shows. This method excludes the risk of selecting only one individual into the stock.

As far as the model is concerned, it is of the utmost importance to retain a wide range and diversity of variations, as such a system can easily adapt to the frequently and rapidly changing economic conditions. It is true in the case of the environment as well. The economy is also characterized by constantly changing economic, social and legislative regulations. Let us take for example the changing legislative regulations arising from the increasing demands of the social lobbying groups and more and more sophisticated raw materials or production technologies.

The basis of the selective process is the basis of the fitness value. As has already been mentioned in this thesis, the fitness function is not closely linked with the burden on the environment. As a result of this, during the selection process the variations that are environmental friendly are not given preference, thus, they do not have better chances for selection. This fact has an unfavorable impact on the expected operation of our model. There are two ways of avoiding this negative effect:

- the external factors can be changed by external interventions (stronger and stricter state control, better quality of the supplied raw materials, etc.) in order to change the genetic diversity of the population and in this way to make the system shift in the optimum direction;
- the selection probability of the environmentally friendly variations can be increased by, internal regulations, i.e. the application of the discriminative

method. Although after making this step the explanation force of our model can decrease, the potential extent of the minimal burden on the environment can be determined ensuring a base of comparison for actual (local) and global optimums

### **2.3. The Recombination**

Genetic algorithms provide the most important and the widest range of various recombination procedures. The operator of the recombination chooses the method by which a new individual can be developed from one or more old chromosomes, that is from the parents' chromosomes. Parents are selected from the stock designed for replication. We also think that the recombination is the basic step, as the nature of variations of the environmental strategy is determined on the basis of this move, in other words the character of the new ideas and the implementation of the new expectations depend on this move.

*In our case recombination means combination and reconciliation of the elements of the possible environmental strategies in order to implement new and more sophisticated strategies for meeting new expectations.*

On the basis of a one-point strategy a recombination point between 1 and L-1 (L is the length of the chromosome) is selected first, and thus, the point (the boundary of two genes) is determined from which the first genes to the right will belong to the first offspring from one of the parents and the first genes to the left will be distributed to the second offspring. In the case of the other parent the distribution of the genes happens vice versa.

In principle  $n$ -point recombination happens in the same way as the one-point recombination, but instead of selecting one point, an  $n$  point is chosen for breaking the chromosomes.

In the process of uniform recombination each gene is examined and a decision is made as to whether it should be exchanged or not.

Gene-mixed recombination is  $n$ -point recombination further developed, but the deviation is quite different from the ones in the procedures described in this study. In this case recombination can occur only if there is more than one set of parents. Due to the peculiarities of the diagonal method there will be  $i$  descendants if there are  $i$  sets of parents. Thus, this variation does not follow the biological analogue, as this method of proliferation cannot be found in nature.

Retaining some guidelines is of utmost importance when applying economic modeling compared to biological recombination. Uniform recombination meets these requirements, as each of its bits is examined and only after the evaluation is made is a decision taken whether the members of the selected variation should be changed or not. In the course of change it is not the smallest chromosome units, the bits that are to be taken into account, but the genes (making up the strategic units). Otherwise a

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process similar to mutation will occur. It can be regulated less efficiently and its outcome cannot be predicted.

#### **2.4. The Mutation**

The third genetic procedure of the genetic algorithms is mutation. During this the specified gene or the value of one of the elements of the gene changes in the chromosome on a place chosen at random. If the biological genetic processes are economically suitable, the mutation is defined as a 'deliberate' variation of the strategic elements, or an error committed by its own or copied strategy.

*In our model mutation is the planned modification of the element or elements of the environment-based company strategy or changes not planned in advance and modifications arising in the course of strategy implementation.*

The planned changes can be brought about by conditions resulting from unexpected external and internal changes in the micro and macro economy, which lead to reformulation of the meaning of the environmental protection as a company objective. In this case the company fails to develop a complete strategy because of the lack of time and is able to modify only one or a few elements of its strategy-The unplanned modifications result from deficiencies in information flow or other processes of the company or even from not precise copying of strategies of other companies. Thus, the extent of the burden on the environment does not always go with the reduction of the impact of mutation. Despite the fact that the probability of biological mutation is relatively low, its importance cannot be neglected either in the process of evolution or in our model.

In the genetic algorithms the importance of mutation lies in its ability to prevent a too early convergence of the population towards a local optimum and to increase its non-homogeneous character. In this way it produces a counterforce against selective pressure. The favorable impact of mutation lies in the retaining of multi-varieties of strategic variations, thus promoting the possible global optimal point.

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## **VALUES AND ENVIRONMENTALLY CONSCIOUS BEHAVIOUR (ECB)**

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*Global environmental problems, depletion of resources, damages to the environment and overpopulation are considered to be the most important challenges of our post-modern age. Environmentally conscious marketing (ECM), using the results of other disciplines, is looking for answers to the above mentioned critical questions. Therefore ECM must concentrate on establish new environmentally conscious consumption patterns or at least changing the existing consumption patterns into a more environmentally-benign way parallel to greening the corporate behaviour patterns as well. That is why understanding consumer behaviour, analysing and predicting values, attitudes and motivation are of utmost importance. In this article the focus will be placed on values since these are considered to be as special filters in environmental conscious behaviour. Comparison of values regarding Eastern vs. Western cultures, or economically developed versus not developed countries is one of the most interesting sides of researches into environmental values. A Global Environmental Survey was carried out in several countries between 1997 and 1999. One of its main objective was to explore and analyse the differences in environmental values of the countries involved in the project. It made me possible to carry out a comparative analysis regarding the Schwartz value structure and Dominant Social Paradigm (DSP) versus New Environmental Paradigm (NEP) in Hungary. The outcomes of my research are quite surprising as the value structure of our students was almost completely different from that of Western or Eastern cultures, and that assumed and expected before the research. The characteristics and possible roots of the distinctions experienced in the Hungarian value structure will be shown in details here in this article.*

Environmental values play an important role in environmentally conscious behaviour as they are considered to be as special filters. Kaiser, Wölfling és Fuhrer (1999) have empirically justified that values have impact on ECB through environmentally-conscious behaviour intention. It was later reconfirmed by the outcomes of my own research carried out among the students of the University of Miskolc in 2004. Other aspects of this survey were to analyse the Schwartz value structure as well as to compare the Dominant Social Paradigm (DSP) with the New Environmental Paradigm (NEP).

There is no universal value definition in the marketing literature. According to Peter-Olson (1987) values 'are cognitive aspect of consumers' needs and desires.'. While Schwartz and Bilsky (1987) define value as '... a belief about a desirable end-state that transcends specific situations and guides selection of behaviour.'

Cross cultural comparison of values is one of the most important aspects of environmental value surveys. The comparison has been made on dimensions Eastern versus Western cultures or Economically Developed Nations versus Developing Countries. The starting point of all environmental value surveys is that each culture has its dominant basic values which have been learnt and accepted by everyone during socialisation. These basic values are often mixed with the product benefits in promotions. These basic values determine which product will be popular or at least accepted in a society. It is assumed that in a culture in which environmental values are dominant environmental protection and consumption of green products are also more important. Dominant environmental values can be manifested through environmentally conscious behaviour and green consumption patterns.

The original survey with which my survey was compared was part of an international comparative study entitled GOES (Global Environmental Survey). The survey was carried out in September 1997 in Japan, December 1997 in Bangkok, Thailand, and January 1999 in metropolitan Manila, Philippines, by the National Institute for Environmental Studies of the Japan Environment Agency (now called the Ministry of the Environment). Another team from the Institute for Social Research at Tilburg University in the Netherlands conducted a survey in that country from December 1997 to February 1998. My survey was carried out in the University of Miskolc in September 2004. The sample size was 333 students aged 21-16 years.

The original survey was published in *Human Ecology Review* in 2003. It made me possible to carry out a comparative analysis regarding the Schwartz value structure and Dominant Social Paradigm (DSP) versus New Environmental Paradigm (NEP) in Hungary. In the original research data from international comparison surveys was analysed to explore differences in environmental values amongst Asian and Western countries. It was found that the structure of environmental values in Asian countries differs from those in Western countries. While an environmental way of thinking conforms to traditional Asian values of honouring parents and family security, Western people believe that such thinking opposes their traditional values. These structural differences, which have been documented by White (1967) and by several Japanese researchers (e.g., Watanabe 1995), are confirmed and clarified by the original surveys. The original study reveals the following conclusions. First, in the Netherlands and the United States, environmental values are linked with altruistic values that are perceived as being contrary to traditional values. In Japan, Bangkok, and Manila, environmental values are linked with both traditional and altruistic values. Second, environmental values are contrary to egoistic and progressive values in all surveyed countries. Third, factors encouraging environmental actions differ by country and by type of actions.

White (1967) insisted that the idea of human dominance over nature caused the destruction of nature in Christian countries, but Watanabe (1995) insisted that Japanese people do not have the same concept of nature as Western people. *Shizen*, the word for nature that is currently used in Japan, is borrowed from Chinese and has a different meaning from the Western concept. Most Japanese do not draw a clear

boundary between humans and nature, while Westerners discuss nature in the context of its relationship to humans.

Researchers in western countries have been trying to analyse values in a common framework. Among them, Inglehart (1977, 1981, 1995, 1996), Inglehart and Carballo (1997), and Inglehart and Abramson (1999) found that his postmaterialist thesis was much related to the emerging environmentalism. Both postmaterialism and materialism are distinguished by a combination of items that refer to the condition of democracy. For postmaterialism, it is “giving people more say in important government decisions,” and “protecting freedom of speech;” for materialism, it is “maintaining order” and “fighting rising prices.” Researchers who chose other combinations of “giving people more say in important government decisions” and “maintaining order,” or “protecting freedom of speech” and “fighting rising prices” are categorized as “mixed.” Inglehart used other surveys to show that generational effect and also that the environmental values of a society are affected by its social and economic situation. This thesis is well known and fits well with data at the nation-state level in developed countries. However, there has been much criticism of this thesis. Brechin and Kempton (1994) maintain that this thesis is not appropriate for explaining globally emerging environmentalism, especially in developing countries. (See other criticisms, Brechin and Kempton 1997; Kidd and Lee 1997; Dunlap and Mertig 1997; Pierce 1997, and for Inglehart and others’ responses, see Abramson, 1997; Inglehart and Abramson, 1999).

The postmaterialist thesis is based on Rokeach’s value theory (Rokeach 1973). Schwartz and Blisky also analysed general value structures based on Rokeach’s, using data from five countries and, later, twenty countries (Schwartz and Blisky 1987, 1990; Schwartz 1992); their five-country study included one Asian society, Hong Kong. They found that the value structure was slightly different in the Hong Kong sample from the samples of Western countries, but the values themselves were not different. Specifically, they found that “the meaning of the values and domains were not different for the Hong Kong sample. What differed was the perception of domains as compatible or in conflict. Value domains seen as incompatible in the West were seen as compatible in Hong Kong.” Furthermore, they explain the differences “based on contrasts between Confucianist and Western thought” that can be clarified by “replications (of surveys) in Chinese cultures and studies in Islamic, Buddhist, and other cultures.” A number of researchers have explored values concerning the environment. Dunlap and Van Liere (1978) first proposed the New Environmental Paradigm (NEP), “composed of three distinct dimensions — balance of nature, limits to growth, and anthropocentrism” (Dunlap and Jones 2002). The concepts of NEP contrast popularly accepted worldviews (the dominant social paradigm) that emphasize mass consumption and economic growth. Using a similar framework, Milbrath (1984) compared NEP and the dominant social paradigm in three Western countries: United States, Germany, and the United Kingdom. Karp (1996) tested the relationship between general values and environmental values. The George Mason University group (Stern, Dietz and Kalof 1993; Stern, Dietz 1994; Stern, Dietz and Guagnano, 1995; Stern, Dietz, Kalof and Guagnano 1995; Stern 1998; Stern, Dietz,

Guagnano and Kalof 1999; Stern 2000; Dietz, Kalof and Stern 2002) has been investigating general and environmental values, including NEP. Using NEP and Schwartz's general value items, they derived four factors in the structure of general values. They called these factors biospheric- altruistic, egoistic, openness to change, and traditional (conservative). According to their results, biospheric-altruistic values, egoistic values, and traditional values are significantly correlated with items in the NEP. The components of each of these factors are shown in Table 3 with my own analysis Biospheric-altruistic values include unity with nature, respecting the earth, protecting the environment, and a world at peace, equality, and social justice. Egoistic values include authority, wealth, and influence. Traditional values include honoring parents and elders, family security, and self-discipline. Most research about environmental values has been done in the United States; few studies have been conducted in Asian or European contexts. One exception is the series of comparative studies by Pierce et al. (1987) in which they applied Inglehart's postmaterialist theory and Dunlap's NEP to both Japan and the United States. Japanese respondents showed a higher percentage of acceptance for NEP items, even among the materialist group, than did their counterparts in the United States. The authors reached a very interesting conclusion: "Unlike the United States, then, in Japan the New Environmental Paradigm is not really all that new."

#### **Analysis of the modified version of Schwartz's general value items**

In the original and in my Hungarian survey a modified version of Schwartz's general value items and economy-versus-environment items were used to clarify the value basis of environmental attitudes and proenvironmental behaviour, and to compare these among the study populations. The modified Schwartz items were developed by the George Mason University group (Stern, Dietz and Kalof 1993; Stern, Dietz and Guagnano 1995) into a twelve-item system that is especially relevant to environmental attitudes and behaviour. Biospheric values include unity with nature, respecting the earth, protecting the environment, while altruistic values include a world at peace, equality, and social justice. Egoistic values include authority, wealth, and influence. Traditional values include honouring parents and elders, family security, and self-discipline.

In the original survey Japan and Thailand were compared because they are the only countries in Asia where the main religion is Buddhism, and because they have not been colonized by Western countries in the past (although Japan was occupied by the United States after World War II for six years). Thailand is categorized as a newly industrialized economic society. There is still a big economic gap between the two countries, which was tried to reconcile by using a sample from the so-called "new middle class" in Thailand. The Philippines is the only country in Asia where the main religion is Catholicism (82% of respondents). Its history is complicated. It had no national king before being colonized, first by Spain, and then by the United States, briefly by Japan in World War II, and again briefly by the United States before independence. The country is very much influenced by American culture. Because the schools teach in English, all of our interviews there were conducted in English.



Hungary is considered to be a developing country, where the main religion is Catholicism. It is worth mentioning that between 1945 and 1989 the number of atheists was significantly increased. After the transition the American and Western European culture significantly affected Hungary. So I assumed that the Hungarian value structure might be similar to that of the Philippines besides the obvious cultural differences and the big geographical distance between the two countries. Therefore *I hypothesized that the value structure of the Hungarian youths shall be similar as that of the Philippines, which is a newly industrialised, ex-colonised, developing country with significant American cultural effects, where the main religion is the Catholicism. So traditional and egoist values shall compose distinct factors, while biospheric and egoist values shall be in the same factor.*

## Results

I asked respondents to evaluate each of twelve general value items with the following question: "Please tell me how important each of these is as a guiding principle in your life." I asked respondents to rate the importance on a fivepoint scale from "completely unimportant" to "extremely important," and included the voluntary options, "this item is against my (respondent's) principles" and "don't know."

	Values	Value category	mean	St dev
1	family security	traditional	4,92	0,45
2	honouring parents and elders	traditional	4,27	0,78
3	self-discipline	traditional	3,86	0,81
4	a world at peace	altruist	4,03	1,02
5	social justice	altruist	3,88	0,86
6	unity with nature	biospheric	3,83	0,90
7	equality	altruist	3,75	1,02
8	respecting the earth	biospheric	3,65	1,02
9	wealth	egoist	3,41	0,95
10	authority	egoist	2,37	1,16
11	influence	egoist	2,69	1,09
12	protecting the environment	biospheric	4,18	0,82

Table 1 - Descriptive statistics of the modified version of Schwartz's general value items, n=333, 2004

Descriptive statistical analyses revealed that the most important value was family security, followed by honouring parents and elders and protecting the environment. These strength of these values were ranged from very important to extremely important. The least important value was authority, influence and wealth. These values were not so important for the Hungarian respondents. Considering the fact that my respondents were university students studying economics, and presumably they are the next generation of company managers and staff, these results are more than a big surprise.

<b>Descriptives</b>			
	mean	St. dev.	N
Altruist values	3,88	0,72	333
Biospheric values	3,89	0,77	333
Traditional values	4,35	0,53	333
Egoist values	2,83	0,88	333

Table 2 – Importance of value factors

Table 2 shows that traditional values are determiners in the life of my respondents, while biospheric and altruist values are equally important, and egoist values are not important at all.

I applied factor analysis to categorize the general value items. The previous results for each country are shown in Table 3, together with those of the U.S. samples by the George Mason University group (Stern, Dietz, and Guagnano 1995) for reference. By using factor analysis, for each country three factors with eigenvalues larger than 1 were derived.

Japan*	Factor-weight	Holland*	Factor weights	USA*, ***	Factor-weight	Thailand*	Factor-weight	Philippines*	Factor-weight	Hungary**	Factor-weight
<i>Factor 1 – Biospheric-traditional</i>		<b>Factor 1 – Biospheric-altruist</b>		<b>Factor 1 - Biospheric-altruist</b>		<i>Factor 1 – Biospheric-altruist</i>		<i>Factor 1 – Traditional</i>		<i>Factor 1 - Biospheric</i>	
A world at peace	0,79	Respecting the Earth	0,72	Unity with nature	0,81	Unity with nature	0,80	Family security	0,85	Unity with nature	0,83
Family security	0,87	Unity with nature	0,70	Respecting the Earth	0,74	Self discipline	0,72	Honouring parents and elders	0,76	Respecting the Earth	0,79
Respecting the Earth	0,65	Protecting the environment	0,63	Protecting the environment	0,81	Protecting the environment	0,63	Self discipline	0,71	Protecting the environment	0,79
Protecting the environment	0,61	Social justice	0,53	A world at peace	0,69	Equality	0,61	A world at peace	0,66		
Honouring parents and elders	0,46	A world at peace	0,52	Equality	0,64						
		Equality	0,48	Social justice	0,59 0,55						
				<b>Helpfulness</b>							
				<b>World of beauty</b>	0,53						
				<i>Belonginess</i>	0,43						
Eigenvalue	3,308	Eigenvalue	3,038			Eigenvalue	3,496	Eigenvalue	4,064	Eigenvalue	3,760
<i>Factor 2 - Altruist</i>		<i>Factor 2 - Egoist</i>		<i>Factor 2 - Egoist</i>		<i>Factor 2 - Traditional</i>		<i>Factor 2 - Biospheric-altruist</i>		<i>Factor 2 – Traditional-altruist</i>	
Influence	0,62	Authority	0,79	Authority	0,67	Family security	0,76	Social justice	0,68	Honouring parents and elders	0,83
Equality	0,58	Influence	0,76	Wealth	0,48	Respecting the Earth	0,63	Unity with nature	0,68	Family security	0,68
Self discipline	0,58	Self discipline	0,30	Influence	0,44	Honouring parents and elders	0,63	Equality	0,62	A world at peace	0,61
Social justice	0,56				0,62	A world at peace	0,60	Respecting the Earth	0,49	Social justice	0,50
				<b>Social power</b>							
Unity with nature	0,52					Social justice	0,49			Self discipline	0,49
										Equality	0,45
Eigenvalue	1,342	Eigenvalue	1,452			Eigenvalue	1,617	Eigenvalue	1,545	Eigenvalue	2,123

<b>Factor 3 - Egoist</b>		<i>Factor 3 - Traditional</i>		<i>Factor 3 - Traditional</i>		<i>Factor 3 - Egoist</i>		<i>Factor 3 - Egoist</i>		<i>Factor 3 - Egoist</i>	
Wealth	0,79	Family security	0,72	Honouring parents and elders	0,85	Authority	0,78	Wealth	0,73	Authority	0,86
Authority	0,78	Wealth	0,66	Family security	0,62	Influence	0,70	Authority	0,70	Influence	0,84
		Honouring parents and elders	0,52	Self discipline	0,56	Wealth	0,62	Influence	0,68	Wealth	0,73
				<b>Honesty</b>	<i>0,71</i>						
				<i>Obedience</i>	<i>0,54</i>						
				<i>Orderliness</i>	<i>0,49</i>						
				<i>Politeness</i>	<i>0,46</i>						
				<i>Social order</i>	<i>0,46</i>						
				<i>Loyalty</i>	<i>0,40</i>						
	1,097		1,151				1,160		1,102		1,078
	48%		47%				52%		56%		58%

\* Source: Aoyagi-Usui, Vinken és Kuribayashi (2003), Human Ecology Review, Vol. 10, No. 1, \*\* my own research in Hungary, \*\*\* George Mason University Group results (see Stern, Dietz és Guagnano, 1995). This survey included more than 12 items. Extra items are put in *italics*.

Table 3- Schwartz's value items factor components (method: Principal Factor Analysis)

KMO and Bartlett test confirmed that factor analysis is a proper method in this case.

<b>KMO &amp; Bartlett test</b>	
Kaiser-Meyer-Olkin measure	,809
Bartlett test and estimated Chi-square	1136,098
Degree of freedom	66
significance	,000

Table 4 – Results of KMO and Bartlett-test

The three result-factors are explaining 58,012 % of whole variance, which is at an adequate level.

<b>Whole variance explained</b>									
Components	Initial eigenvalues			Sum of square factor weights			Sum of square rotated factor weights		
	total	variancia %	cumulated %	total	variancia %	cumulated %	total	variancia %	cumulated %
1	3,760	31,336	31,336	3,760	31,336	31,336	2,413	20,107	20,107
2	2,123	17,690	49,026	2,123	17,690	49,026	2,373	19,777	39,884
3	1,078	8,986	58,012	1,078	8,986	58,012	2,175	18,128	58,012
4	,858	7,154	65,166						
5	,735	6,126	71,292						
6	,655	5,460	76,752						
7	,625	5,206	81,958						
8	,578	4,817	86,775						
9	,456	3,797	90,572						
10	,422	3,519	94,091						
11	,368	3,069	97,160						
12	,341	2,840	100,000						

Table 5 – explained variance (Method. Principle Factor Analyses (PFA))

The result-factors are as follows:

values	Factor components		
	biospheric	Traditionalist- altruist	egoist
family security	0,19	0,68	0,23
honouring parents and elders	0,00	0,83	0,09
self-discipline	0,27	0,49	0,21
a world at peace	0,28	0,61	-0,27
social justice	0,42	0,50	0,07
unity with nature	0,83	0,15	0,05
equality	0,36	0,45	0,07
respecting the earth	0,79	0,21	-0,12
wealth	-0,01	0,18	0,73
authority	0,02	0,02	0,86
influence	0,04	0,06	0,84
protecting the environment	0,79	0,22	0,07

*Method. Principle Factor Analyses (PFA), Rotation: VARIMAX with Kaiser normalisation. Number of iteration. 5.*

Table 6 - Rotated component matrix

The three components, showing the value structure of our marketing students, resulting from the factor analysis is unique as the Hungarian value structure is not similar to any of those countries also involved in the surveys.

- Biospheric values can be found in a distinct factor-component only in Hungary. In any other cases these values are mixed with other values. In countries representing the Western cultures (USA and the Netherlands), in the Philippines (maybe due to the American effect) and even in Thailand biospheric values are mixed with altruist ones in a single factor-component, while in Japan biospheric values are linked to traditional ones.
- Traditional and altruist values can be found in the same component only in Hungary.

In Table 3 the different factor components of values for each country are clearly shown. For Japan's data, factor 1 was labelled as "biospheric-tradition" because it includes two items of tradition and two environmental items. Factor 2 was labelled "altruistic" because three altruistic items are included, although one was related to the environment (unity with nature). Factor 3 was labelled "egoistic," which includes wealth and authority. For the data from the Netherlands and the United States, three environment-related items (respecting the earth, unity with nature, and protecting the environment) were grouped with altruistic items such as social justice, a world at peace, and equality. But in Japan, they were grouped differently. Factor 1 was labelled as biospheric-altruistic, factor 2 as egoistic, and factor 3 as tradition. Table 3

also compares responses from the Asian countries. In all three countries, environment-related items were categorized differently. In Japan, two environment-related items were grouped with the traditional items, and another one with altruistic items. In Bangkok and Manila, two environment-related items were grouped with altruistic items, and another one with traditional items. In all three countries, the egoistic items were in a separate category. The results suggest that the structure of values might be different in non-Western countries, as Schwartz found. Environmental values are not distinct from altruistic or traditional items. Thus, as Pierce et al. (1987) reported, the NEP concepts may not be new among Asian people. The environment is tightly connected with other value items. But the structure does not seem to be the same, even among Asian countries. The close relationship of traditional and environmental values was observed in Japan, but not in Bangkok or Manila.

As I mentioned before, my survey in Hungary revealed a unique value structure as biospheric and egoist values composed different factor components, while altruist and traditional values were mixed in a third, separated component. Therefore my hypothesis must be rejected.

The three factor components made it possible for me to show them in a 3D-like chart. In Chart 1 biospheric and egoist values are shown very far from each other, whilst altruist and traditional values are close to one another. The structure of the values in Hungary has serious marketing consequences. Since in our country the biospheric values are distinct from other values, environmental arguments used to enhance environmentally conscious behaviour should be based on biospheric values and they should not be mixed with other (i. g. arguments based on traditional or altruist values) arguments. This reasoning was later reconfirmed by the results of a questionnaire survey on individual waste collection behaviour for Miskolc Regional Waste Management Project. Phone interviews of more than 800 people living in the region covered by the project revealed that the most important motivation factor in selective waste collection was environmental value-based. Every other motivation factor can be neglected (see Chart 2)





### Why participating in selective waste collection?

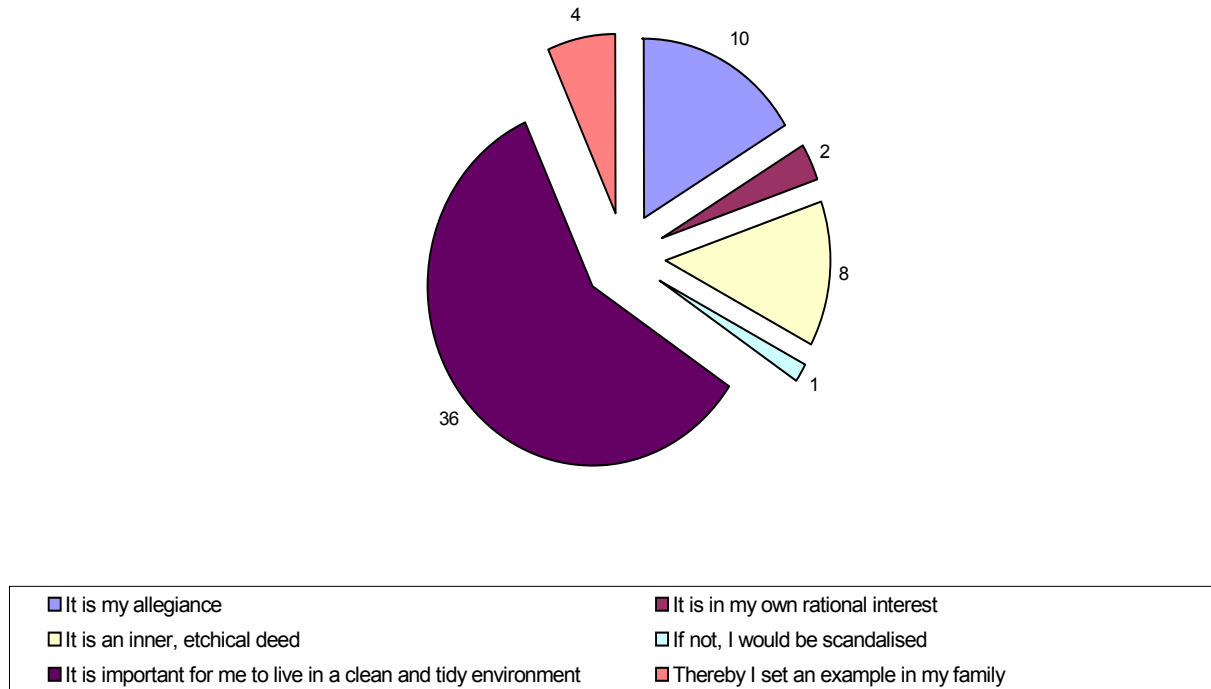


Chart 2 – Motivation factors of participating in selective waste collection, Miskolc, n=800, 2004

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## **CHANGE MANAGEMENT IN THE BACKSTAGE OF CRM PROJECTS**

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### **Preamble**

Between 2001-2004 the Institute of Management Science at the University of Miskolc worked on a research. Within the compass of it the Institute accepted to inquire several Hungarian companies making representative sample of their function in several years' retrospect by using EFQM model as the basis of the research. The judgment of the participant companies occurs on compliance with it and it gives the best method to measure competitiveness and prominence of the companies' consideration of which shouldn't neglected after the EU formation.

Serving the aim of the research the employees of the institute drew up the questionnaire consisting of eleven chapters, which maps every field of activity of the participant companies. The first chapter of the questionnaire, "Customer Satisfaction", was edited according to the customer satisfaction of the EFQM model. Its main aim is to introduce the basic points of external customer satisfaction. We tried to enquire whether the customer is inspected in the companies and if the conscious customer care runs, if yes – on what level? The modern CRM (Customer Relationship Management), which was also inquired in earlier research, had an important role during creation of the questionnaire. The degree at which the companies meet these kinds of requirements should be taken into a count. In chapter "Customer Satisfaction", nine questions were comprehended then posed and organized. The questions were the following:

- 1) Do people conduct the customer satisfaction survey?
- 2) Is the conscious customer care in the companies?
- 3) Do they investigate the annual rate of losing customers, if yes – what is it?
- 4) What is the annual rate of new customers inside all the customers?
- 5) How do they inform their customers about new products and services?
- 6) Do they consider the customer demands?
- 7) Do they have permanent connection with clients through a channel?
- 8) Do they provide any training services?
- 9) Do they meet the deadline for delivering and keeping guarantee according to the schedule?

### ***The results of the research***

On the base measurements we approach to the numerous conclusions, in which there can be found the following facts:

- only 65-70% of the companies conduct a customer satisfaction services, most of which did it once of casually
- conscious customer-treatment means registering purchases for 40-45% and only 23-30% provide customer satisfaction services and conscious customer information
- two thirds of the companies (65-67%) does not investigate the reasons and rates of losing customers
- 40-60% of the companies does not realize the ratio of new customers in circle of all customers
- changes of customers' demand are not followed by 15-25% of companies at all, but even those who do it carry out only random surveys (30% - producers and 60% - suppliers)
- 55-75% does not provide any training services

Considering the above results it can be concluded that the companies in our country are not ready for promoting the right-level customer-relations and to satisfy customer demands at the profitable level. The best solution would be to conduct the modern CRM systems using which some improvements can be reached but the conduction should happen only according to the capacity of the different companies. But there can be greater problems due to the lack of funds and the directors of medium companies do not realize the opportunities given by the modern CRM system. In the next four lines we sum up the main opportunities which are offered by the modern customer care solution of the companies.

CRM gives new policy to client-treatment, which is makes more and more companies to understand the importance of customer care policy. Essentially we need the information about customer satisfaction.

The number of those companies that use developed and up to date solutions for customer care is still insignificant and more than 1/3<sup>rd</sup> of the companies do not realize that the CRM can be as a basic strategy in their functioning.<sup>1</sup>

### **Elements of CRM**

The main aim is to achieve higher efficiency in client-treatment, which would mean more effective communication and stronger connection among partners, faster decision-making process and immediate market-response and more efficient control. Due to the abovementioned factors productivity level may increase; companies' images might be ameliorated and subsequently this may result a higher economical functioning; they also might strengthen companies in their market places.

The following 4 elements should be attentively managed in order to achieve our aim:

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<sup>1</sup> <http://www.icon.hu/hirek/rolunk/crm.html>

1. **CRM Strategy:** competitive strategy in companies for management of client-connections;
2. **CRM Information Processes in company:** multifunctional processes for a contact management at concerned and other companies;
3. **Purchasing of technological tools for CRM Support:** tools for communication with clients, for computerizing, storing and analyzing of data, which is needed in contact management;
4. **CRM Human Resources:** workers necessary for operation;

This is important to make director of each company to be aware CRM significance. It is not just software or a software-package. All of the four elements should be put together in order to achieve the result.

### ***CRM Technical Components***

Almost every information field might be visible during the client-treatment in spite of the fact that integration is increasing in the field of technical tools. Only one complex, well-organized system can serve each field of a contact management.

Organization of the information system can be started after fulfilling the conditions. The CRM information system has three main components according to the META group:

#### ***a) Operational CRM***

The main task is to provide technical support of direct management by the help of information science. It performs integrated and continuous collection of data meanwhile consolidating information. Information of client interactions, which are coming from the outer channels, is managed, recorded and computerized by the Operational CRM system. The system supports tasks from related functional fields like Implementation, client service and marketing. Operational CRM systems are able to report a wide range of client data, but they cannot be used for information analysis. The first and the most important system's task to support daily operational duties (marketing, Implementation, client service, production development) of contact management.

#### ***b) Analytic CRM***

Due to the analysis of customer information collected by the operational CRM software and other outer data sources such knowledge can be gained, which can give significant advantage for the organization in any field of contact management. Reports are able to facilitate company management providing further advantages: observation of client segmentation; client dropout is a potential task of marketing. Realizations based on the purchasing models provide significant information for realization. Amount of complaints in different regions has high importance in the

terms of customer care. It should be mentioned that system helps on the way of company's strategy Implementation. Nevertheless analytical methods should be realized only after setting up the Operational CRM System.

**c) *Interactive/Collaborative CRM***

Perhaps this field of information technology develops most rapidly nowadays. Spread and development of mobile tools are significant for those merchants who are working in the field of Implementation. On-line mobile networking and Internet connection spread widely. Off-line network with a central database plays important role in providing extensive data safety and extending mobile tools accessibility. (<http://www.euronetrt.hu/megoldas/megoldkezd.htm>)

*The base of contact management – Database Creation*

Applied information technology is developing continuously, because of increasing information demand. Research in the form of computerized data recording system is the main technological tool of marketing. Central database is the core of CRM System. It contains all the data types for its clients. System's structure might be kept in the same way for several months and years if hard work is needed during that period of time. Results can be obtained in a long period of time.

In fact, contact management is being held at any company. For example, clients' bases are formed where clients' names, addresses and phone numbers are stored. Majority of companies save information about their clients, but this information gathered and kept in companies' independent databases mostly. (Mártonffy A)

*Companies involved in introduction to the CRM*

The main aims of corporative management are to maximize the number of clients, profit and to increase the income. CRM projects should be started within narrow bounds inside the company and shouldn't be announced to the whole company. First of all, available company sources should be estimated and after then missing lines should be supplied. There is no need to replace every functional part. Request can only be hold by results and profit funds. Consultants who are working on the introduction of CRM system define Main areas of CRM project:

- marketing
- selling
- customer service

Besides abovementioned there are some other important fields:

- financial
- delivery section
- channels of customer connection (sales, internet, phone)
- strategic and operational (support and process systems)
- data collection (information warehouse)



*Purposes and timing of CRM introduction*

There are three main purposes:

- complicated competition
- client-keeping economical policy
- more effective and profitable technical implementation

Evidently, CRM Advantages can be found in its final results: profitable achievements, improved performance and satisfaction of employees and clients.

These aims show that task of the company is long-lasting client care.

Implementation of CRM System offers the following:

- minimized costs
- maximized profits due to more efficient realization
- increase of profit due to client-keeping policy <sup>2</sup>

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<sup>2</sup> <http://www.cognos.hu/megoldasok/crm.htm>

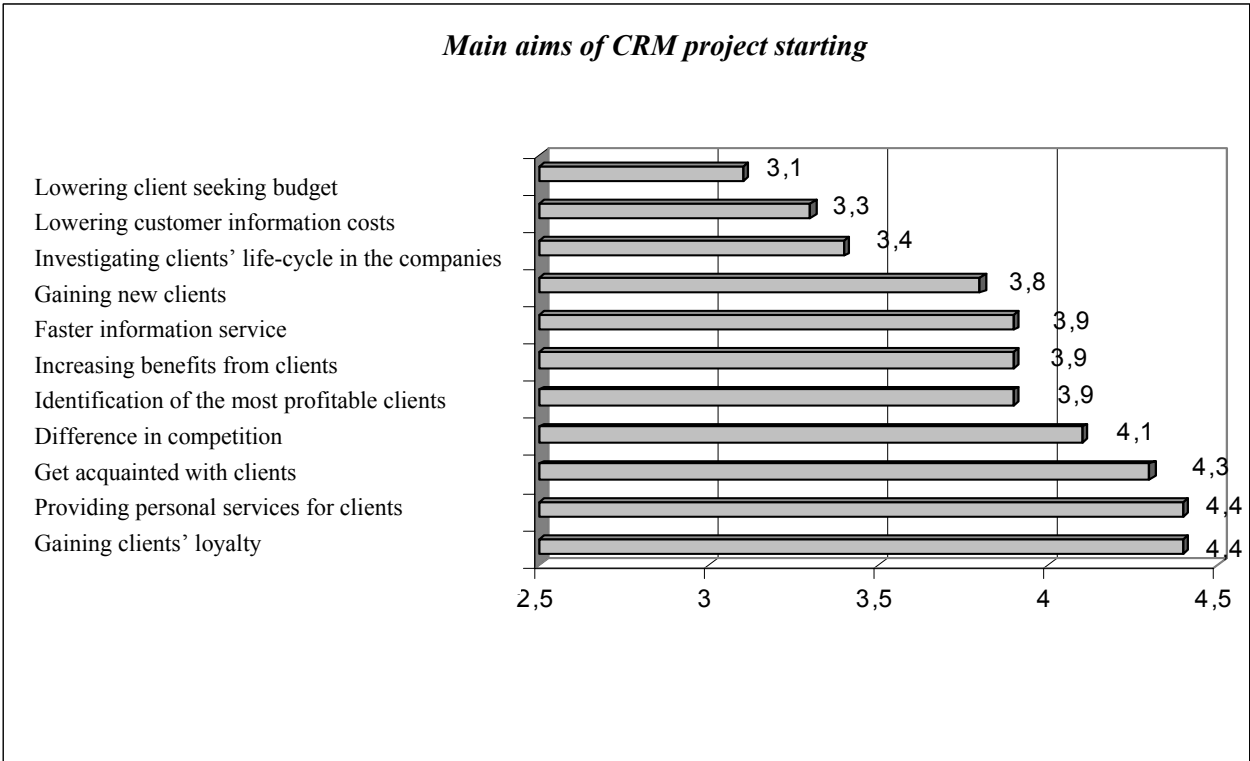


Figure 1

Source: IDC és Cap Gemini, 1999

**Conditions of CRM introduction**

Two main basic factors:

- 1) A company needs a great client-circle and the ratio between costs and clients should be low.
- 2) The clients should be registered by names

According to general opinion the CRM touches four sectors (telecommunication, banking, other services, production companies) but all sectors can raise the necessary funds to finance the introduction to CRM. Probably the first two sectors will introduce the project as soon as possible because they have acceptable number of clients; essential financial funds and they are able to take effective customer care, which is required in strong competitive situation.

Nowadays it is an outdated fact that most of deputy-directors and directors do not take part in project management. The rapid development of technology and communication has made the changes and strategy modification an everyday topic. As for strategy modification the most effective tool is the project management, which concentrates on organization of human resources, information and relevant methodological and technical tools. Project manager is the person who is responsible for project fulfillment and has got adequate authority.

The project duration varies according to its size and complexity. In fact each project as well as CRM follows a certain cycle, which is called the project life-cycle and it means that every project consist of parts built on each other. The structure of the project should be arranged due to complexity and renovation. The procedure is determined by three main principles:

- taking to section parts
- progress from comprehensive to detailed approach
- problem solving cycle

The different phases of the project depend on distribution of sections from the project main points and complexity. Nevertheless the practice shows that we can divide phases into four essential parts:

- 1. Project definition, 2. Planning phase, 3. Implementation, 4. Closing phase

At the very beginning of the project introduction problem solving possibilities should be kept in view and every phases should be carefully worked-out because a thoughtless planning can result disappointment. Striving for topicality is essential as the world is always changing. An adequate project management is needed to be deductive. Every phase of the project based on its preceding phase. These accounts', while the possibilities of influencing project results are decreasing, costs are increasing.

### Change Management in the backstage of the CRM projects

Whether it's an upgraded or new CRM system, a drive to get more out of existing technology or even a change in the philosophy of CRM for the company, it all requires some form of change management.

The changes are different according to their signification in the organization and their situation in the work of the leaders. Boody and Buchanan (1992) co-operated with project managers in different changes. The examination of these changes recommended that 2 dimensions should separate the project:

First: how central place does the change have according to the most important work of the organization? (Key process/marginal)

Second: how new is it in that environment (classification from the “new” to the “known”)

The new process is likely to meet barrels and it is more than the marginal ones. On 1<sup>st</sup> quarter of the 3<sup>rd</sup> diagram the change is new, but takes its place in the edges as we look at the main tasks of the organization. So here, the effect of the change on the person's vulnerability is low. The change of the 2<sup>nd</sup> quarter takes its place on the edges and is known in the given practice. The change of the 3<sup>rd</sup> quarter is known, taken from existing practices but it has an influence on key processes of the organization. It can be a challenge – if successful – can endanger the basic business activity.

The changes of the 4<sup>th</sup> quarter are those, which have influence on the key processes, and for the given knowledge they have a significant content. These are the most difficult from all the changes. These change projects can move among the quarters, like the employees, who gain more experience. By our experience this is typical in the cases of different CRM projects, which began in the 1<sup>st</sup> or the 3<sup>rd</sup> quarter.

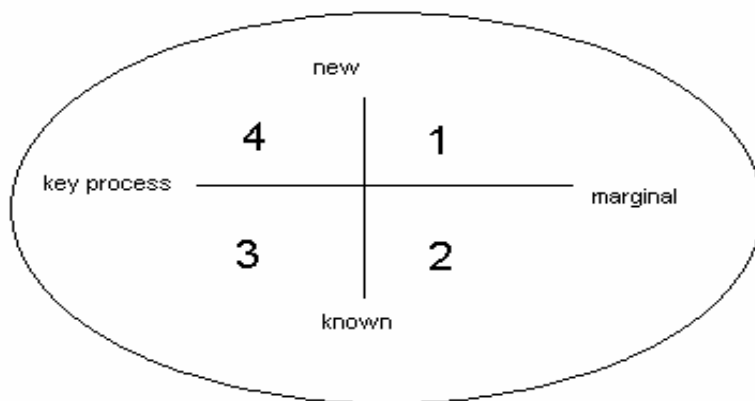


Figure 2:  
The two dimension of the two projects

The CRM objectives, goals and vision have been developed and understood by all senior management personnel, start the communication process with the rest of the organization to begin to deal with and help overcome both rational and emotional resistance. You need to be able to relate what the roll out of CRM technology is going to mean to your business and how it is going to affect the overall performance of the business. Following this it is important for the CRM Project Team to start developing the CRM journey map or plan. This will include (Stewart):

- Translating the strategic requirements into bite size tactical initiatives. Do not try the big bang approach; get some runs on the board first with achieving the most critical requirements first and building on this success.
- Mapping requirements--start at the end and move backwards. Start with the desired outcome, data requirements, process enhancements (changes or new introductions) and the impact on people and their roles. If you cannot clearly describe how the desired outcome is going to be used to manage the business through a formal process, ask yourselves why do it at all?
- Technical partner selection. Choose partners not just suppliers as CRM is a journey, it is an ongoing initiative so be sure your technology is supplied by an organization that not only has the technology now but a vision for the future that closely aligns with yours.
- Change and communication. How is it going to be managed on an ongoing basis and does the organization possess the skill sets (and dedicated focus) to continue to get the most out of the system from a people, process and technology point of view?
- Develop Performance Measures for the CRM, including:
  - The technical development and implementation
  - The CRM system performance
  - The impact on the business: efficiency and effectiveness
  - The users: in-putters and report runners
  - The customer: How has the CRM journey impacted them?
  - The "partners": How have they performed to expectations?

### ***Change Step-by-step for CRM***

A decision to change is made. This decision is to implement CRM. This should, however, be made only after careful consideration that your strategic initiatives and goals are going to be achieved through the implementation of CRM or a new CRM philosophy. After the analysis of many international and well known methodological approaches applied by consultants - with respect to both the common and country specific characteristics – a new project was born that can be applied in Hungary as series of methodological steps.

The steps can be used as phases of a project in practice. Each level means a milestone in the project and all the levels can be further itemized. The table 1. contains the steps and the main tasks of the project.

<i>Steps</i>	<i>Tasks</i>
<b>1. Preparation</b>	<ul style="list-style-type: none"> <li>• Recognizing the need for changes</li> <li>• Define your strategic CRM objectives, goals and vision</li> <li>• Forming the leading guiding committee</li> <li>• Vision, general aims</li> <li>• Forming the team in charge of planning</li> <li>• CRM project team development, team education</li> <li>• Accepting the operation model of the modification</li> </ul>
<b>2. Situation inquiry, identification of the processes</b>	<ul style="list-style-type: none"> <li>• Detailed determination of the customer demand</li> <li>• Identification of the processes</li> <li>• Determining the business strategic needs</li> <li>• Initial success</li> <li>• Preparing the flow chart</li> </ul>
<b>3. Understanding and analyzing the processes</b>	<ul style="list-style-type: none"> <li>• Understanding the structure of the processes and procedures</li> <li>• Determining the value increasing activities</li> <li>• Benchmarking</li> <li>• Problem solving processes</li> </ul>
<b>4. Aims of processes</b>	<ul style="list-style-type: none"> <li>• Assessing the opportunities</li> <li>• Detailed definition of CRM aims</li> <li>• Approval of the leading committee</li> </ul>
<b>5. Planning new processes</b>	<ul style="list-style-type: none"> <li>• Structure of the new process</li> <li>• Analyzing the information demand</li> <li>• Choosing the appropriate alternative</li> </ul>
<b>6. Technical planning</b>	<ul style="list-style-type: none"> <li>• Understand and identify the technology will enable the CRM objectives and goals to be achieved</li> <li>• IT planning</li> <li>• Defining the establishment</li> <li>• Introduction plan</li> </ul>
<b>7. Planning of human resources</b>	<ul style="list-style-type: none"> <li>• Determining the tasks and labor demand</li> <li>• Determining the needs for management and directing</li> <li>• Planning the new organization and sphere of activity</li> <li>• Communication of changes</li> <li>• Education plan</li> <li>• Planning the changes of the system of incentives</li> <li>• Planning the temporary organization</li> </ul>
<b>8. Implementation</b>	<ul style="list-style-type: none"> <li>• Continuous communication</li> </ul>

	<ul style="list-style-type: none"> <li>• Assessing the inclination to changes of the employers</li> <li>• Implementation of the technical planning</li> <li>• Education</li> <li>• Plans of control and implementation</li> <li>• Experimental introduction</li> <li>• Gradual or complete introduction</li> </ul>
<b>9. Assessment of the changes</b>	<ul style="list-style-type: none"> <li>• Analyzing and assessing the CRM change</li> <li>• Systematic research of further improvement opportunities</li> </ul>

Table 1: Steps of the CRM Process Improvement method

The steps have been planned as phases of a process change project for more successful practical use. The connection of the 4 project management phases and the 9 main steps are as follows:

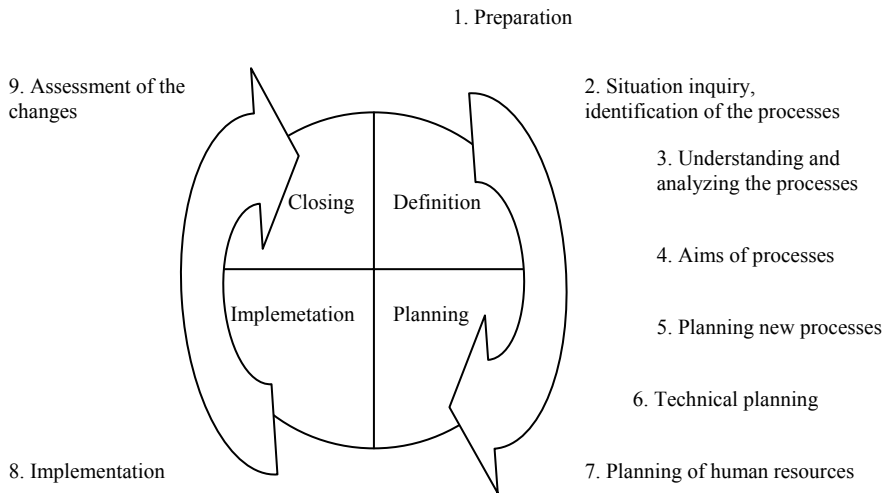


Figure 3: The steps and the project phases

The change steps are all about getting staff to a level of competence in a managed and sustainable fashion. It's about understanding what is really happening to staff and the organization during a CRM project and the changes these types of projects involve. These are not things that can be easily understood or identified by most organizations so get some expert help as it will pay dividends in the long run. Knowing what to do when and how through the use of a change model like the Steps of the CRM Process Improvement method will help ensure greater CRM successes!

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## **BIRTH AND FERTILITY RATES IN HUNGARY IN THE 20TH CENTURY**

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Primarily data of the exact birth and fertility rates on the present territory of Hungary were first recorded in 1876. According to them the first decline in fertility rate was seen in the middle of 1880s.

Taking into consideration the demographic trends in Europe the 47‰ crude birth rate recorded in 1876 in Hungary was considered high. Every year this figure slightly dropped by 0.288 per thousand point (0.674%) and by the turn of the century it was under 40‰. The average number of children born per family amounted to 5 (5.3), which was sufficient to replace the population, although both child and infant mortality rates were high.

The fertility rate slightly decreased in the first half of the 20th century. In the period between 1900 and 1914 the crude birth rates dropped by 0.33 per thousand point (1.059%) every year and in average the drop was 14%. In the years before the First World War 34 children were born alive to 1000 women.

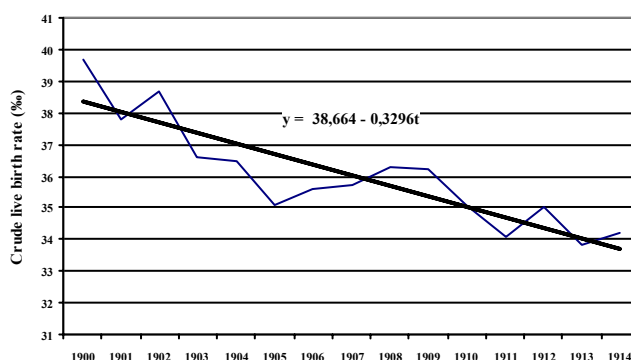


Figure 1. Crude live birth rates in Hungary between 1900 and 1914

The trend in fertility rate in Hungary is worth comparing to trends in other European countries. In the years before the First World War the European crude live birth rates can be divided into three groups:

Countries with high fertility rates: The crude live fertility rates in these countries were above 35‰. This group includes Eastern and south-eastern European countries (European areas of Russia, Romania, Bulgaria, Yugoslavia and Hungary)

Countries with intermediate fertility rates: The crude live fertility rates in these countries were 25-35‰. This group comprises most Central and Southern European

countries (Austria, the Netherlands, Check Republic, Germany, Italy, Portugal and Spain)

Countries with low fertility rates: The crude live fertility rate in these countries was under 25%. Northern and Western European countries belong to this group (Belgium, United Kingdom and Sweden)

In the years before the First World War for a quarter of a century the decline in fertility was very characteristic of Europe but its extent varied. The crude live fertility rates were rapidly decreasing in England, Hungary, France and Germany, but in other countries with high fertility rates there was hardly any noticeable decline.

The First World War had a long lasting impact on the development of Hungarian and European population. During the war years there was a considerable deficiency in birth rates accompanied by a temporal decline in the number of population. The crude live birth rate in Hungary showed all time low record in 1918. The live birth rate was 16.3 children per 1000 women. In the period between 1915 and 1919 the number of born children was lower by 40% than 5 years before and by 36% than five years later, i.e. in 1920-1924. This decline in the birth rate was one of the highest in the countries taking part in the war. The neutral countries did not experience such a drop.

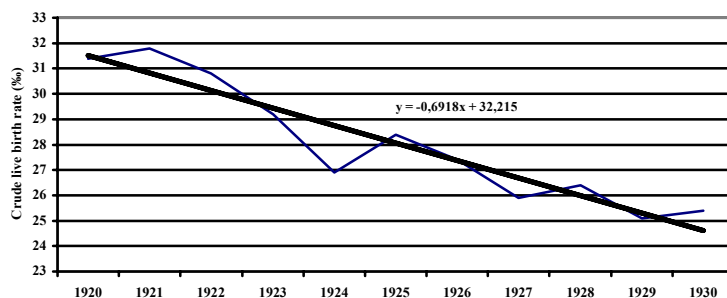


Figure 2. Crude live birth rates in Hungary between 1920 and 1930

In the post war period there was a temporal boom in the birth rate, but it was not as high as in the years before the war. In Hungary the highest crude birth rate was seen in 1921 when this figure reached 31.8%. In the early 1920s the total fertility rate was only 3.8. There was a further decline in fertility rate started in the 1880s. Between 1920 and 1930 the crude fertility rate decreased by 0.69 points (2.098%) every year. In 1930 the total fertility rate was 2.8, which was hardly the half of the rate computed at the turn of the century.

The changes experienced in Hungary were similar to the changes in the countries taking part in the war. The increase seen in 1919 reached all time high record in the years between 1920 and 1922. The baby-boom followed by a decrease happened in a different way in certain European countries. In most Western European countries the

dramatic drop in the birth rates started in 1922 or 1923 (France, Belgium and Germany). In Central and Eastern Europe the birth rate was considerably high and levelled off at that time.

The beginning of the 1930 saw a dramatic decrease in the fertility rate. It was the period of economic recession in the world. In 1930 and 1936 the crude birth rate in Hungary declined by 20%. Between 1930 and 1940 the crude birth rate dropped by 0.54 point (2.362%) every year.

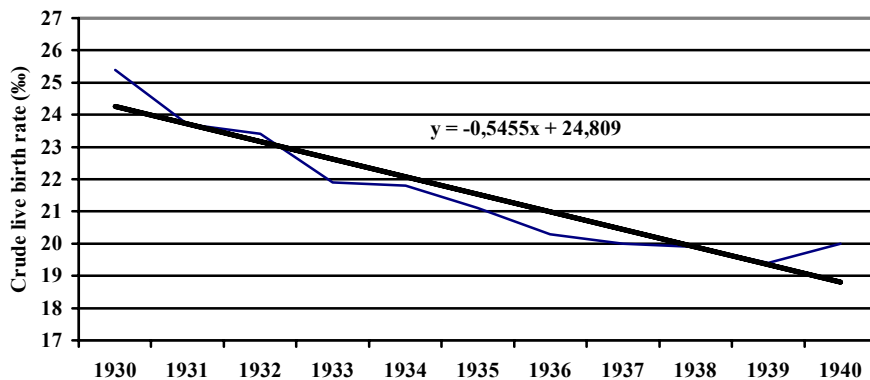


Figure 3. Crude live birth rates in Hungary between 1930 and 1940

As it has already been mentioned above the decline in the fertility rate was not a unique trend in Europe, but its pace was very dramatic. Although in the years before the First World War the birth rate in Hungary was considered to be quite high, in the late 1930s it was very low. The decline in the crude birth rates in European countries in different periods is shown in the box-plot. In Hungary this figure was 45.3‰ in 1876-1885, which was considered the highest in Europe, but in 1908-1913 the rate was only 35.1‰ and Hungary was rated somewhere in the median and third quartiles in Europe. While there was a further decrease in the fertility rate in European countries, the relative position of Hungary was also changing. According to figures of 1920-1924 and 1930-1934 Hungary took the middle position on the list of the European countries. In 1940-1944 it slid back to position in the second quarter having only 19.7‰ of its birth rate.

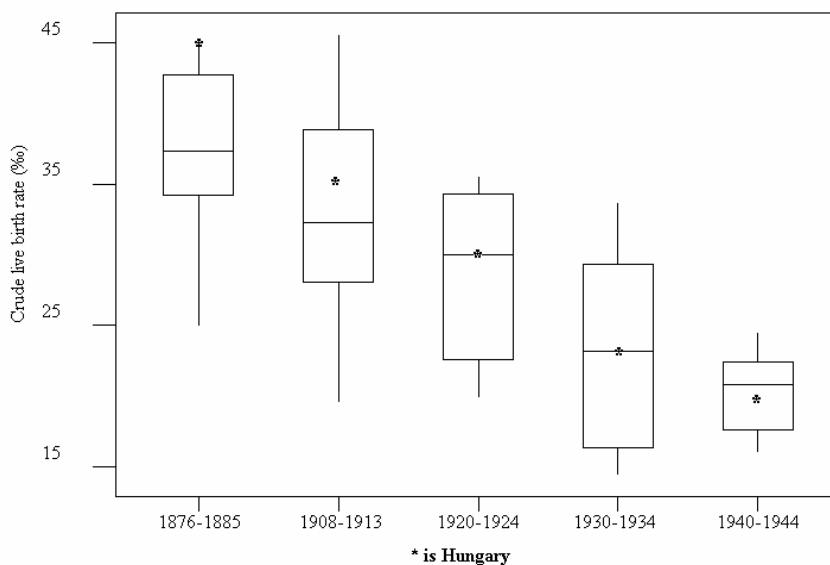


Figure 4. Box-plot figures showing the birth rates in European countries at different periods

The reduction in the fertility rate can be explained by the economic recession. It can be the result of the increasing number of employed in industry, the growing urbanisation trend, the increasing education level and the employment of woman workforce. The ongoing changes, the economic slump as well as the changes in fertility had various impacts on different social classes. The number of children among white colour workers and those employed in industry was gradually decreasing. On the other hand, in families involved in agriculture this figure levelled off and corresponded to the number computed at the turn of the century.

The decline in fertility rate depended on the age of women as well. The average decrease in fertility can be explained by the change in the behaviour of older women of childbearing age, which led to reduction of the ones undertaking more children.

The analysis of the live birth rates per 1000 women by age in 1901-1940 shows the decrease of birth rates in all age groups. The extent of the decline differed in various age groups. The slightest decline in fertility rate was observed in the youngest group. The older the women became, the more considerable decrease in the fertility rate was recorded.

Age groups of women [year]	1901 - 1931	
	Total change [%]	Annual average change [%]
15-19	-34,06	-1,38
20-24	-39,84	-1,68
25-29	-47,98	-2,15
30-39	-52,73	-2,47
40-49	-64,05	-3,35

Table 1. Live birth rates to 1000 women of child bearing age between 1901 and 1931

Age group of women [year]	1931 - 1941	
	Total change [%]	Annual average change [%]
15-19	-2,61	-0,26
20-24	-6,27	-0,65
25-29	-6,66	-0,69
30-34	-13,45	-1,44
35-40	-24,33	-2,75
41-49	-19,87	-2,19

Table 2. Live birth rates to 1000 women of child bearing age between 1931 and 1941

This led to the decrease in the importance of various age groups and to the change in the fertility structure. Before the First World War two groups were the most fertile, namely the fertility of women aged 25-29 was considerably higher than those of 20-24. On the other hand, in the years before the Second World War this figure was only 85% compared to 20-24-year old women.

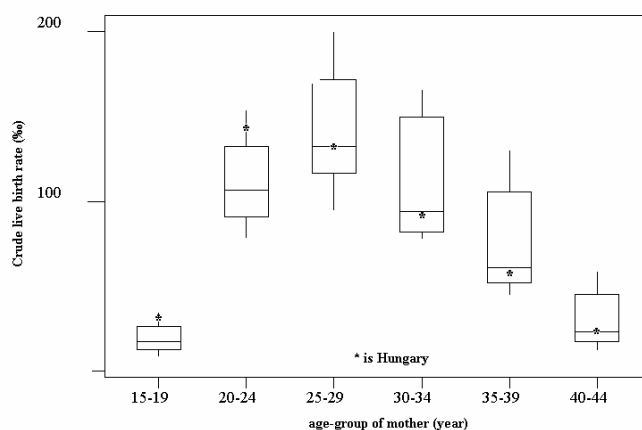


Figure 5. Box-plot figures showing the live birth rates to 1000 women in Europe in late 1930s

In the early 1940s there was a slowdown in the decline of the fertility rate in Hungary. The fact that the low number of women born in the First World War entered the child bearing age and had an impact on the trend in the birth rate should not be neglected. The Second World War did not cause as much shortage in the birth rate as the First one. In the years to follow there was not such a considerable increase in the figures either. The birth rate gradually increased until the early 1950s

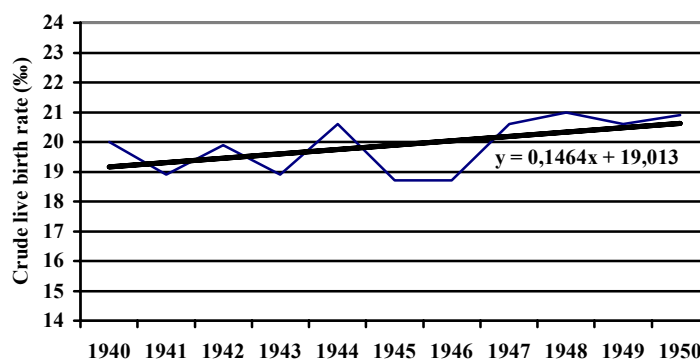


Figure 6. Crude live birth rates in Hungary between 1940 and 1950

From 1950 the fertility rate started to decrease again and attracted the attention of the government of that time. The strict measures taken in order to prohibit abortion had a favourable impact on the birth rate and resulted in a record number of births in 1954.

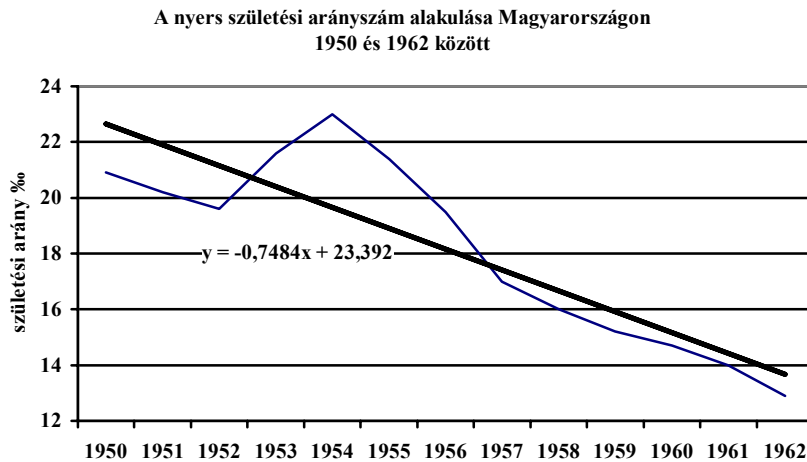


Figure 7. Crude live birth rates in Hungary between 1950 and 1962

After the ban on abortion was lifted the most liberal law with respect to abortion was passed. This move resulted in a considerable decline in the fertility rate. After reaching the peak in 1954 the birth rate dramatically dropped in 1962 and bottomed out at 12.9%. This figure was considered the lowest in the world. Between 1954 and 1962 the crude birth rate decreased in average by 7% every year and there was a total drop of 44%. The number of the children born in 1962 was lower by 93.3 thousand people (130,053 people) than the generation in 1954. This number was a little higher (2159 people) than the figure registered in 1918 when the birth rate was the lowest (127,894 people). The total fertility rate in this period decreased from 3.0 to 1.8. The drop in the fertility rate in Hungary started much earlier than in the western societies. The decrease in the birth rates in Europe after the Second World War was experienced in Hungary first and dropped under the reproductive level.

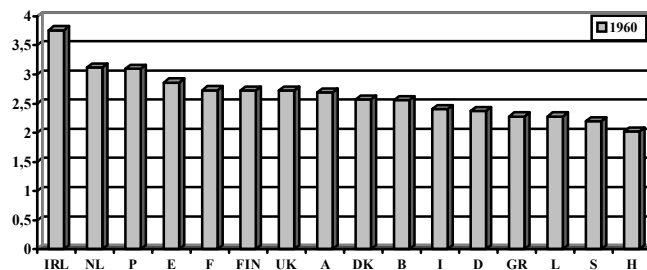


Figure 8. The total fertility rate in the Western Europe and Hungary in 1960

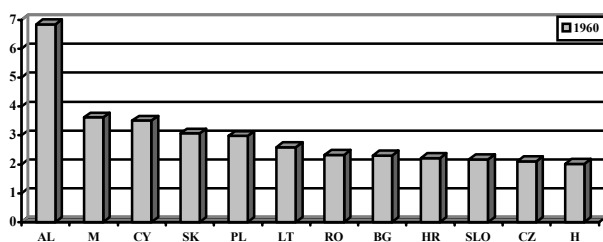


Figure 9. The total fertility rate in the Eastern Europe and Hungary in 1960

The decline in the fertility rate was observed in all age groups of women. The considerable decrease in the birth rate can only partly be explained by the liberalisation of abortion. It must be noted that in 1957 there was a drop of 13.3% in the birth rate compared to the year before. A more dramatic decline was seen only during the First World War, in 1915 and 1916 and a similar decrease was experienced in the Second World War, in 1945. Among the reasons leading to this drop there were social and economic changes, namely almost full employment of women, the development of a stereotype family with two breadwinners and better qualified women.

As the majority of children were born to breadwinning mothers, there was a contradiction between the role of a mother and the role of an employee. The solution to this problem was looked at and found in overcoming this contradiction. As a result the child care allowance system was introduced in 1967. After its introduction both the birth rate and the total fertility rate slightly increased, but it was followed by further decline and stagnation.

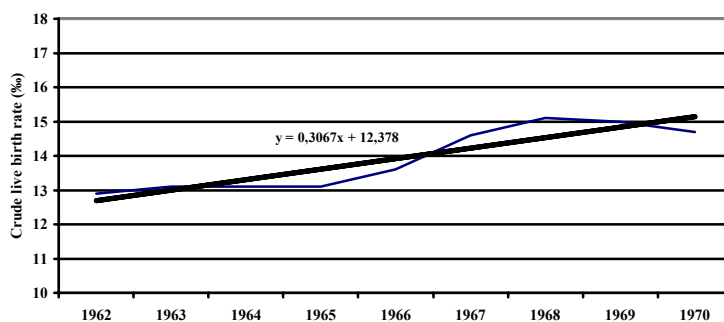


Figure 10. The crude live birth rate in Hungary between 1962 and 1970

Although another complex package encouraging birth was introduced in 1973, the increase in fertility rate was not sustainable. It lasted several years and was only



slightly above the reproductive level. 1975 saw all time high record when 194,240 children were born. The crude birth rate amounted to 18.4‰. The total fertility rate peaked at 2.38, which hardly corresponded to the simple reproductive level. This favourable move was accompanied by the fact that the high number of women born in the years of strict abortion entered their child bearing age. This fact cannot be neglected. After 1975 there was a dramatic decrease in the birth rate. Between 1975 and 1980 the annual birth rate decreased by 25%, which corresponded to an annual drop of 5.2%.

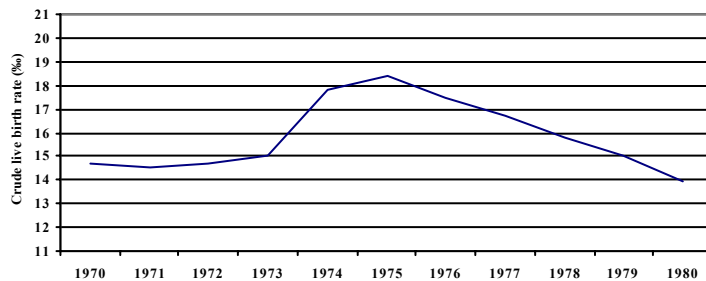


Figure 11. The crude live birth rate in Hungary between 1970 and 1980

In 1984 there was another bottoming out as only 125,359 children were born. This figure was lower by 35% than the all time high record in 1975 and by 3.6% lower than the one in 1962. In 1984 the live birthright per 1000 women was 11.8‰ and the total fertility rate was only 1.73. These figures led to the introduction of the child care allowance system, which targeted better qualified and well paid women force. As a result the decline in the live birth rate stopped for a while at 12‰ and levelled off until 1990.

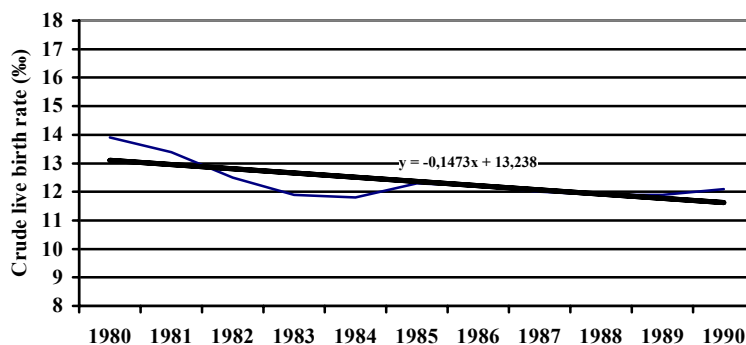


Figure 12. The crude live birth rate in Hungary between 1980 and 1990

The early 1990s saw a dramatic decline in the fertility rate. The live birth rate dropped by 25% during this period and fell under the psychological limit of 100,000 people in 1998. It was the result of the fact that from the middle of the decade the high number of women born 20 years ago entered their most fertile period. Thus, the number of women aged 20-29 gradually increased and at the turn of the century their number was higher by 160,000 people than 10 years ago. The increase in the number of women of childbearing age did not lead to the increase in the willingness to give birth to more children. The total fertility rate during the whole decade declined by 30% and in 1999 it dropped to 1.29. It means that the number of the growing generation was lower by about 40% than the number of their parents. Although there was a slight increase in the fertility in 2000, it was not steady. In the past several years the fertility has been levelling off.

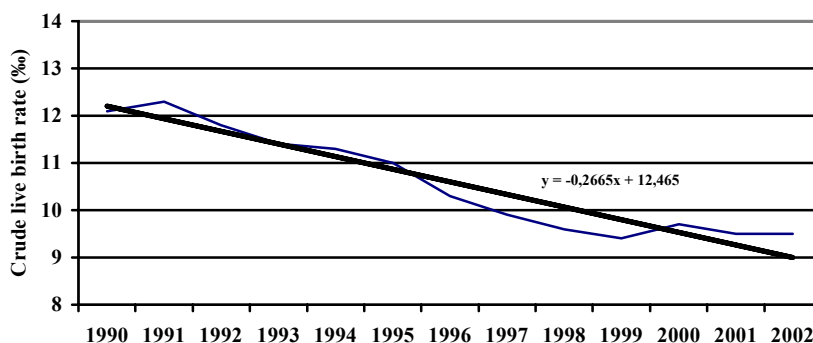


Figure 13. The crude live birth rate in Hungary between 1990 and 2002

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**THE NEW STANDARD REGULATIONS OF IFRSS (INTERNATIONAL FINANCIAL REPORTING STANDARDS) TO APPLY FROM 2005**

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**Presentation**

In this study I would show the certain elements of changes implemented in IFRSs. As it is known, the consolidated financial statements of the entities whose securities are publicly traded from 2005, must be compiled according to the regulations of the IFRSs.

For the widespread adoption of IFRSs as a global accounting regulation, persistent improvements are needed, the most important milestones of this process being the changes applied from 2005, which were determined by the correspondence of EU expectations and the increasing full-scale acceptance of US stock exchange.

According to these aims, the reduction of the number of the alternative treatments was persisting, and more elements appeared which are known from the US GAAP regulation system.

The aim of this study is certainly not the holistic presentation of the changes, but the emphasize of those items which demonstrate the direction of changes or which resulted in remarkable changes in principle.

Considering that the IFRSs are close to the point of being the only financial statements preparing principle, and that – in case of quoted businesses- they are becoming the integrated part of the Hungarian Accounting Law, the trend and the alteration of these accounting principles can be very useful for those interested in dealing with financial statements of corporations. Hereafter these changes are going to be detailed according to certain topics.

**1. Changing of departures connectid with fair presentation**

One element of the standardization of financial statements is to restrict the possibility of departures from IFRSs. According to the new regulations, one can depart from the standards and interpretations only in extremely rare circumstances, only if the adaptation of it would hurt the principle of fair disclosures.

Naturally, in case of deviation, the companies have obligation for disclosures. With this modification, the standardization principle of financial statements has become stronger.

**2. Changes in Presentation**

In the field of compiling financial statements, some more changes were done, which are good to know for the readers of the balance sheet in the interest of better

understanding. During the compiling of the balance, current/non current presentation has become principle.

The former possibility was limited to introducing the asset-liability items in order of liquidity, if it results in presentation that is more reliable.

In practice, the possibility that the presentation in order of liquidity is reliable, can arise in the case of liquidation of a company. So in the future, we can hardly meet non short- and long-term expiration differentiation.

It is a very important change as well, that the extraordinary item is prohibited, so in financial statements prepared according to the IFRSs, extraordinary items will not be presented.

Among the changes of presentation it is worth emphasizing that in the Profit and Loss Statement or in the Statement of Changes in Equity, the minority interests and the interests of equity holders must be shown separately.

### **3. Usage of LIFO cost formula**

One step to the unified evaluation system can be that the usage of the LIFO (last-in, first-out) cost formula is not allowed anymore by the relevant standard. So another new alternative treatment has been abandoned by the IFRSs.

### **4. Accounting policies, changes in accounting estimates, errors**

Reading the accounting financial statements, it is very important to know how to show the possible events of the previous period in due form. According to the IFRSs, these fields are the modification of accounting policies, changes in the possible accounting estimations, and the errors of the previous period. Earlier, alternative treatments fitted in with the differing accounting practice of the different countries in this field. The modified standard deleted the alternative solutions. According to the new regulations, the possible modification of the accounting policies and the correction of the errors must be presented retrospectively.

The details of its can not be presented in this study, but the aim of the modification is to help the understanding of the readers by compiling the relevant year and the comparative period based on similar valuation method.

### **5. Residual value**

A specification took place in the area of the fixed assets, which is an interesting theoretical question to be interpreted according to the IFRSs. Naturally, according to this standard's instructions, the amortization of the tangible assets and the intangible assets has to be determined by the respect of the residual value.

The different accounting regulations define other ways to establish residual value. In IFRSs, residual value is the price the asset would cost at present, if it had achieved end of its useful life, I.e., one does not have to deal with the prospective change of

value, usually we take into consideration the similar assets at the end of the period of use as residual value.

## **6. Amortization of idle assets**

Further specification took place also in the area of fixed assets, which deals with another accounting theoretical question. In the life of companies it is part of the natural operation that certain assets become idle, but the realization does not occur or the recently purchased asset is still or temporarily not available for use for production. In this case, physical use does not continue, and the recovery of the asset does not continue as well. Under these circumstances it can arise whether to continue the amortization – until the derecognizing or activation- or to cease the settlement of amortization. IFRSS chose – in contrast with other frequent accounting regulation and professional practice – to continue the amortization until derecognizing.

## **7. Component approach**

The component approach is the regulation-level acceptance of that often occurring case when some assets are compiled from different, easily separated components. (Frequently mentioned example for this is the aircraft and its internal accessories). These different components have to be treated in different ways. So the amortization has to be determined by the given component's characteristics (useful life), but their renewal, their exchange and their derecognizing is going to be accounted in terms of the component and not of the asset.

## **8. Differentiation between land and building**

By now several questions were introduced, which can give an unequivocal and logical instruction for the regulation of certain area, considering the principle of fair presentation. This specifying change- appearing as if particulars - but still showing the complex quality of IFRSSs, can be connected to leasing. Leasing of the real estates take place very often, where the leasing includes both the value of the land and the building.

In this case, leasing of the land and leasing of the building has to be differentiated, according to the fair value of the two elements. In case of land, considering that the time of use is essentially indefinite, financial and operational leasing criteria cannot be used. The leasing of land can be classified as a financial leasing only if at the end of the leasing the land is going to be our property, in all other cases it must be treated as an operative leasing. The building-part of the leasing – according to the normal leasing classifying rule – can be treated as either financial or operative leasing.

## **9. Disclosure requirements concerning related parties**

The disclosure of transactions with related parties is an important area of every accounting regulation, because settlements with related parties can divert the financial

statements of the given company from the market conditions and through this, business and financial independence of the given company can be assessed.

Though several small modifications occurred, one particular area shall be highlighted in this topic. Probably due to former experiences, the effecting range has been expanded. The modified standard has recognized the fact that not just the private individual owners and the management of the companies, but the family members of these persons can be in a business relationship with the company, and this fact can be an interesting detail for those reading the balance sheet for making their decisions. Therefore the modified standard has extended its influence to close family members of private individuals possessing essential influence and with to key persons' closest family members of the company and its parent company as well. Hereby from 2005, information on relationships with these private individuals can be gathered from these financial statements.

### **10. Intangible assets, impairment of assets**

I would discuss the highlighted changes of areas regulated by these two different standards in one chapter, because in case of impairment the changes to be introduced can be connected to intangible assets.

In case of intangible assets, assets with indefinite useful life have appeared as a new item. The rules of US GAAP had acknowledged earlier, that in the property of the company there could be intangible assets, where the useful life cannot be determined. This possibility is acknowledged by the modified IFRSs, with the supposition that in this case the time of use is indefinite.

With these assets – taking into consideration the supposition of indefinite useful life – the amortization will not be settled. At the end of the year, the useful life has to be reconsidered. If the time of use becomes determinable, then thereafter the settlement of amortization has to be defined, as if it is an account estimation change.

Naturally, the company has to give rationale for why the given asset is considered to have an indefinite useful life.

The relief of the useful life limitation is the supposition that the intangible assets' time of use is no longer than 20 years has been eliminated.

Moreover, further specifications have been made in the determination of right-supported assets' useful life.

In the new regulations, time of use cannot be longer than the time of right in case of these assets. On the other hand if the company has convincing proof about the probably shorter useful life, in the aspect of amortization, a shorter useful life can be taken into consideration.

In case of such assets, the tenor of right of the company can be potentially lengthened. This further tenor can be part of the useful life only if we have an opportunity to prolong it with a minimal extra expenditure, in which case we can suppose that the lengthening is going to be realized.

The other topic to discuss in this chapter is the modification of the standard regulating the impairment's accounts. Among these modifications, those assets have been determined, where the testing of the impairment happens annually. The possible impairment has to be tested every year at intangible assets with undetermined lifetime –introduced above - and at the non-finished intangible assets and also at goodwill.

In case of goodwill, the standard contains further instructions for the accounts of impairment. The impairment of goodwill is different from the other assets' impairment. The goodwill – according to the IFRSs rules as well – arises at the accounts of business combinations. Briefly, the goodwill is the difference between the cost of business combination and the buyer's share from net assets of the acquisition. The goodwill - arising like this - cannot be classified independently as a difference; its recovery and its impairment depend on other assets, or group of assets.

In case of immaterial goods, the accounts of impairment are done according to the IAS 36 impairment of assets standard. This standard deals with intangible assets, tangible assets and with certain accounts connected with financial instruments.

In the following, it is worth introducing the common principle of the standard.

Impairment has to be accounted for – according to the standard – if the carrying amount of assets is above the recoverable value. The recoverable value is the higher of the fair value less costs to sell and the value in use.

Fair value less costs to sell is the amount obtainable from the sale of an asset or cash-generating unit in an arm's length transaction between knowledgeable, willing parties, less costs of disposal.

Value in use is the present value of the future cash flows expected to be derived from an asset or cash-generating unit.

The calculation of the prospective cash-flow has to be based on the company's latest financial plan. The prediction has to include the following 5 years, the further periods have to be taken into consideration with the extension of this 5 years' data – the most convenient is the growth rate used one.

At the determination of the 5 years, it was taken into consideration that in normal case after this period the data can be given only with great uncertainty.

An external factor which accounts for revision is, for example, the decline of market value; the changes of technological, market, economical, and legal environment; the increase of influential interest rates – which was taken into consideration at the discount-, and when the carrying amount of the company's net assets are more than the company's market capital value.

Internal factors referring to impairment are for example: obsolescing, physical damage, changes or probable changes in the use of the asset (i.e. the earlier sale of the asset than it was scheduled, halt or reconstruction of the factory), and if the internal reporting system provides information referring to impairment.

The company has to review every year whether there is a starting-point to determine that the earlier accounted impairment does not exist any more. For making this, the

company has to take into consideration internal and external factors- similar to the existence of impairment.

The probable reversal of the impairment's reasons has to be taken into consideration in that category, which was the basis of impairment's accounts. For example if the basis of impairment loss was the value in use, then - among others - the interest can be the watched/monitored factor, whereas if the fair value was considered, then the market prices can be the indicators of impairment's restore.

The accounts of impairment in some cases cannot be connected to individual assets, only to some group of assets. For example, at certain production lines, contribution amount can be determined only for the whole production line. The smallest group of those properties of which asset influence is independent from other properties, or group of properties, the standard calls them cash-generating units.

If the carrying amount of properties belonging to the cash-generating unit is lower than the recoverable amount, then impairment has to be accounted for. During the impairment first the goodwill – belonging to the cash- generating unit - has to be written – off, and the residue has to be accounted in proportion to the properties of the unit. During the impairment, the individual asset's value cannot reduce under the highest value of the fair value less cost to sell and the value in use.

Naturally, similarly to the individual assets, in case of the cash-generating unit the impairment has to be reversed, if the above mentioned conditions are existing.

The modified standard specifies the way of goodwill's accounting. According to the regulations, the goodwill has to be assigned to the cash-generating unit from the date of the acquisition and this assignment has to be executed by the end of the following business year. The goodwill has to be assigned to the smallest unit which is monitored by the management of the company. This unit cannot be bigger than a financial segment. If more units can profit from the synergic effect of the acquisition, then the goodwill has to be distributed among the units. Hereby the goodwill becomes an integrated part of the assets, and the usual impairment logic can succeed.

Naturally, when the unit is going to be realized, then the goodwill has to be stroked out, or in case of restructuring, the goodwill's allocation has to be done. Mainly in case of goodwill, if the impairment has been accounted for, then in the case of the later periods' changes, the impairment cannot be written-off.



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**REGIONAL DIFFERENCES OF GDP AND UNEMPLOYMENT RATE IN  
SPAIN AND IN HUNGARY  
IN EUROPEAN UNION ENVIRONMENT**

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***Summary***

*The objective of the study is to present the regional differences of GDP and unemployment rate in the different regions of the European Union between 1998 and 2001, paying special attention to the regions of Spain and Hungary. As for the absolute values and the GDP volume, significant differences of the regional GDP data per capita were experienced in the EU25 regions. It has been observed that during the period in question, GDP showed growth while the disparity among countries did as well. As for the unemployment rate, higher disparity was observed during the above mentioned period than GDP. In case of the new member states there was not a region having outstanding rate but unemployment rate grew dramatically in 50% of the regions. Based on my analysis, I drew the following conclusion: Okun's law is not necessarily true at a regional level.*

**1. Regions in the European Union – conditions of regional analysis**

The EU uses the NUTS system (Nomenclature of Territorial Units for Statistics) to compare regions, which – since its foundation (beginning of the 1970s) – has significantly changed. The Committee declared its first Directive in 2001, in which a proposal was made for the determination of the hierarchic structure. The decree itself has been valid since May 2003 (1059/2003) containing the ranking conditions of the regions, the regions of the member states and the exceptions.

Not only the regulation was changed but the determination of the regions also. In 2002 EuroStat published the regional changes of the membership states (1981-1999) on nearly 100 pages. During this period, some countries implemented a complete regional reform, while others changed the name or the code of their regions. Hungary – for example – completed the changes on the micro-regional level in 2003 (NUTS4), meaning that 150 micro-regions were turned into 168, while the 1995 regional system did not change. There has not been a significant change in Spain either since their access to the EU.

On one hand it is understandable to make changes in regional ranking in order to help more efficient improvement in the given country, on the other hand, though, these all make the completion of regional analyses difficult. This problem can be solved with the golden section – not taking minor changes into consideration –, but we must understand that certain changes for which the NUTS system was created cannot be measured correctly. On one hand the problem is about

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<sup>1</sup> Scholarship of the Ministry of Foreign Affairs of Spain, Universidad de Oviedo, Principado de Asturias

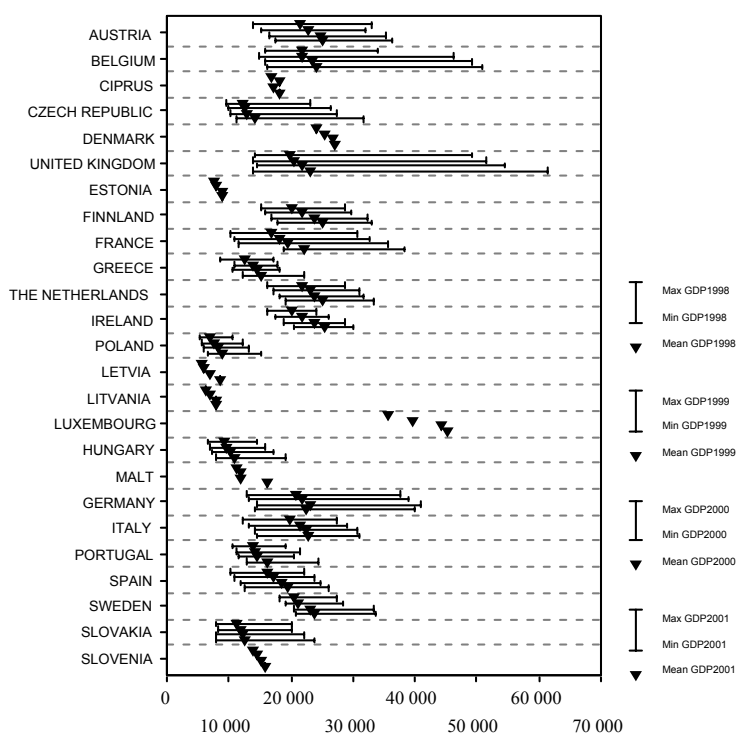
the usability of data, on the other hand the presentation of chronological changes of the given parameters is more difficult.

## 2. The regional distribution of GDP between 1998 and 2001<sup>2</sup>

In the observed period the country with the highest number of regions was Germany, followed by the United Kingdom and France. There were 8 countries having only one region (the regional and the national level were the same).

The next chart illustrates how significant the deviation is in the EU-25 countries. The biggest regional gap (volume) is in the regions of the United Kingdom.

If the average is on the left hand side, there are few regions with high GDP in that country. 12 out of 16 countries having more than two regions show outstanding GDP values compared to the other regions of the country.



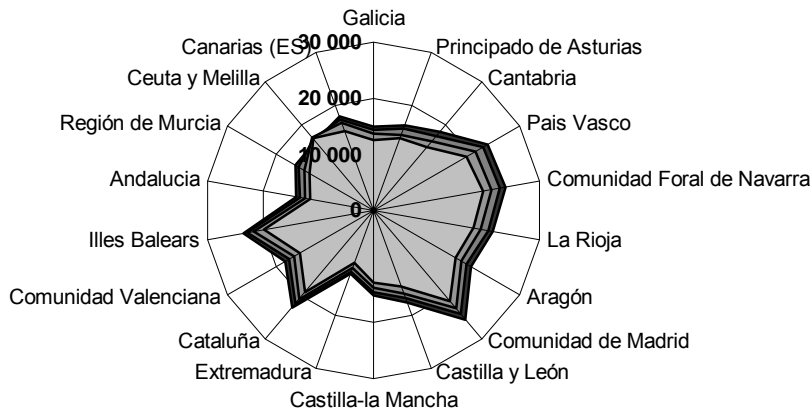
Source: EuroStat; personal chart

Chart 1: The GDP situation of the EU-25 country regions for the years between 1998 and 2001 (from top to bottom)

<sup>2</sup> During the GDP analysis, for the sake of comparison I use the GDP per capita counted at purchase power parity. Due to the lack of comparable regional GDP data, I can only examine the period between 1998 and 2001. Because of the short term, the economic conclusions are not thoroughly based, thus can only be used as guidance.

EU countries can be divided into 3 main groups as far as the regional disparity is concerned. One group, where regional volume grew, is where the leading region grew even stronger. The best example for that is Hungary, where the middle part of the country is continuously gaining advantage. The second category, where the regional differences did not change, only the limit values grew: ex.: Spain. The third group contains those countries where the regional gap decreased in the period observed.

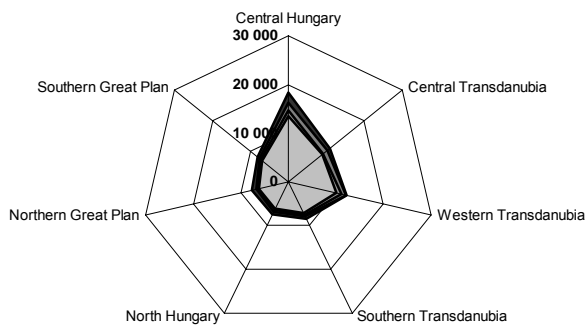
Preparing a separate chart for the GDP values of the Spanish regions, it becomes clear that the GDP changes in the regions is steady. There are no regions with outstanding GDP, which would lead to regional differences as the capital, Madrid does not have outstanding figures. There are some regions, though, where the value of GDP increased slighter than in the other regions: ex.: Asturias.



Source: EuroStat; personal chart

Chart 2: GDP per capita in the regions of Spain  
(the darker the colour, the more number of years passed)

In case of Hungary, the middle of Hungary is clearly the first among the regions, still showing increase. Growth is evanescent in North-Hungary and the North Plain.

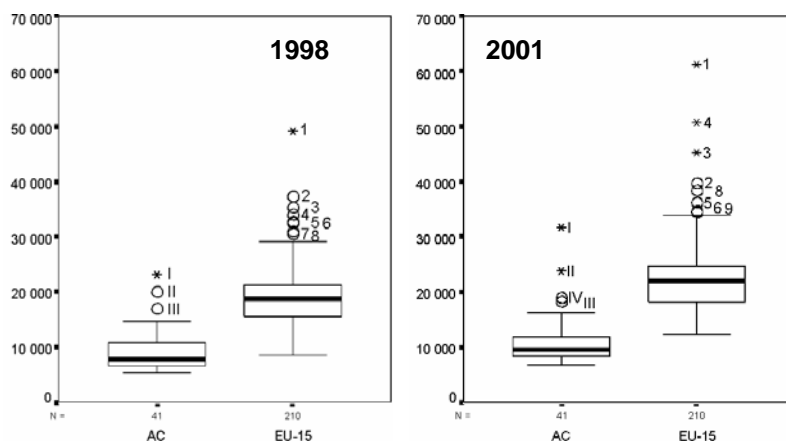


Source: EuroStat; personal chart

Chart 3: GDP per capita in the regions of Hungary  
(the darker the colour, the more number of years passed)

### 2.1 GDP repartition in EU15 and in the new member states

The charts below clearly show us that in GDP volume there is significant difference between the EU-15 regions and those of the new member states. For this reason, I examine the repartition of the „patterns”, from which conclusions can be drawn about the tendency of GDP changes.



Source: EuroStat; personal chart

I=Praha; II=Bratislavský kraj; III=Kypros; IV=Közép-Magyarország; 1=Inner London; 2=Hamburg; 3=Luxembourg (Grand-Duché); 4=Region de Bruxelles; 5=Wien; 6=Oberbayern; 7=Darmstadt; 8=Île de France; 9=Berkshire, Buckinghamshire and Oxfordshire;

Chart 4: GDP per capita in EU-15 and in the 10 new member states

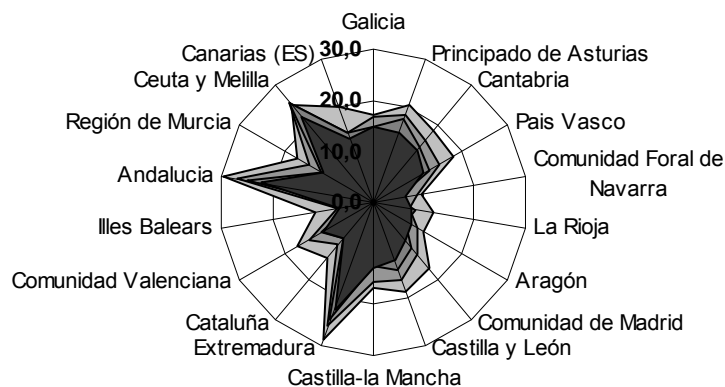
In the observed period, half of the regions of the old member states increased their GDP value and the regions with eminent GDP values are currently in an even more advantageous position. A reverse tendency can be felt in case of the new member states (AC). GDP decreased in half of the regions, although regions in the upper 25% GDP value increased their advantage further together with regions having extreme values. The lower 25% showed slight increase (almost nothing compared to EU regions). Regions with outstanding values increased their advantage by 2001. By 1999 Middle-Hungary is among the extreme values of the new member states, while the absolute rank did not change. This proves that regions having extreme or outstanding values gained more advantage than more than half of the EU and AC regions.

### 3. The repartition of unemployment rate in EU-25 regions

The average unemployment rate in EU15 decreased continuously from 1998, by 2001 it reached 7,6% (EU25 9,2%). The pace of increase was higher in EU15 than in EU25. During the observed period, unemployment rate fell in nearly half of the countries.

The biggest volume was experienced in France and in Italy. France's outstanding value – the highest in EU25 – is assured by the peripheral region. Among the new members, the highest volume is in Slovakia, outrunning even Poland. On average, unemployment rate is high in Slovakia, but there is a region with outstanding results, that of the capital. Thanks to this, the spread of the country's unemployment rate is bigger. Contrary to this, Poland is the only country above the EU average meaning that its region with the lowest unemployment rate has higher national unemployment rate. Other countries are: Estonia, Cyprus, Lithuania, Latvia, but all these countries have only one region.

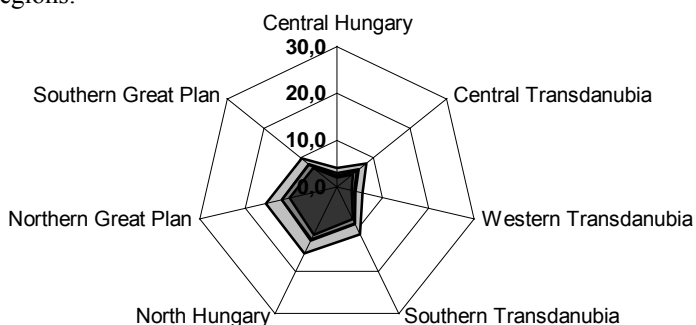
In Spain, regional disparity decreased concerning the unemployment rate and except for one or two regions, the index value decreased proportionately.



Source: EuroStat; personal chart

Chart 5: Unemployment rate in Spain  
(the darker the colour, the more number of years passed)

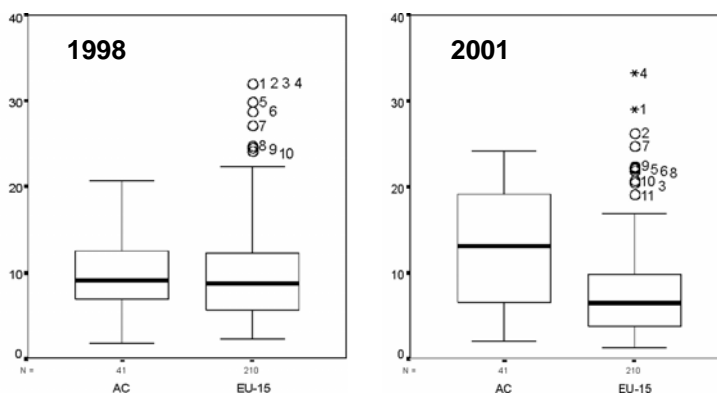
The Hungarian tendency is true for Spain, the only difference being that here unemployment rate decreased more significantly in regions with high value than in the other regions.



Source: EuroStat; personal chart

Chart 6: Unemployment rate in Hungary  
(the darker the colour, the more number of years passed)

If I separate the pattern (AC, EU15) based on the previously used method (AC, EU15), and make a chart with the well-known method, it becomes clear that among the regions of the 10 new member states there are no regions having extreme or outstanding values.



Source: EuroStat; personal chart

1=Guadeloupe; 2=Martinique; 3=Guyane; 4=Réunion; 5=Andalucía; 6=Extremadura;  
7=Calabria; 8=Ceuta & Melilla; 9=Campania; 10=Sicilia; 11=Sardegna

Chart 7: Unemployment rate in EU-15 and  
in the 10 new member states

Regional differences grew in case of the new member states' regions. In 1999, it was sensible that the upper and the lower values changed the same way while disparity grew among 50% of the elements. The same tendency was felt in 2001. While in case of the new member states the regional difference of the unemployment rate increased, in the EU15 regions it decreased. More outstanding values appeared by 1999 and 2001 respectively. In EU15 regions peripheral regions, three Spanish regions and 3 (4 in 2001) Italian regions have the biggest unemployment rate.

#### 4. The close relation between GDP and the unemployment rate at a regional level<sup>3</sup>

As a first step, I examine what correlation exists – if any – between the yearly GDP and unemployment rate at a regional level.<sup>4</sup>

The results show that year-by-year the relation between the two indices is stronger and stronger. The 0,459 value is a relatively strong correlation, and it grew even stronger based on the 2000 data (0,595), although it decreased slightly in 2001. The relation between the indices is negative as the higher the GDP in a region, the lower the unemployment rate is<sup>5</sup>.

<sup>3</sup> I made the analysis with the SPSS 11.5 software and kept the charts in English.

<sup>4</sup> I use the Spearman indicator to define correlation as according to my bibliography, it can be used more efficiently in certain situations as the outstanding values do not affect the indicator value.

<sup>5</sup> But as we have seen, there are exceptions.



As we have NUTS3 level data for Spain and Hungary for the observed period, the analysis of the strength of the relation between the two criteria on NUTS3 level is necessary. The result of the analysis is surprising. If we take the values of the two criteria of the two countries' NUTS3 level regions, the relation is not significant and is positive for 1998!

Chart 1: The summary of the NUTS3 level correlation coefficient between the two observed criteria based on the Spanish and the Hungarian example

Correlation Coefficient Spearman's rho			
	GDP_1998		GDP_1999
Unemp_1998	0,013	Unemp_1999	-0,023
	0,912		0,848
	GDP_2000		GDP_2001
Unemp_2000	-0,123	Unemp_2001	-0,070
	0,303		0,557

On the other hand, if I take the Spanish and the Hungarian patterns separately, the result is very favourable: the direction of the relation is negative, the closeness is very strong and the model itself is very significant.

To continue the original analysis to make a regression analysis, the equation of the regression line for 1998 is:  $GDP^{98} = 21.402 - 389,9Unemp^{98}$ . Thus in 1998 with 95% probability, as a result of a 1% increase in unemployment, GDP value rose on average by  $389,9 \pm 2.63,0$  (in PPS), i.e. by a value between 263,9 and 515,9.

After completing the linear regression analysis for the next three years, it can be stated that the regression line covers the pattern in question in a greater proportion. Both models are significant and I accept the value of the coefficient, it being significant.

So far, I have examined the EU-15's and the new member states' regions. A separate analysis is also worth doing.

Chart 2: The regression analysis of the two criteria in the different regions of the EU15 and the new member states, 2001

Coefficients <sup>a</sup> - EU15			Coefficients <sup>a</sup> - AC		
	Unstandardized Coefficients			Unstandardized Coefficients	
	B	Std. Error		B	Std. Error
(Constant)	25 408,5	728,65	(Constant)	16 805,3	1 374,17
Unemp2001	-403,0	77,62	Unemp2001	-424,7	92,57

a. Dependent Variable: GDP2001

In both cases, the model is significant and the equations of the regression lines are:

$$GDP2001EU = 25.408 - 403,0Unemp2001EU ,$$

$$GDP2001AC = 16.805 - 424,7Unemp2001AC .$$

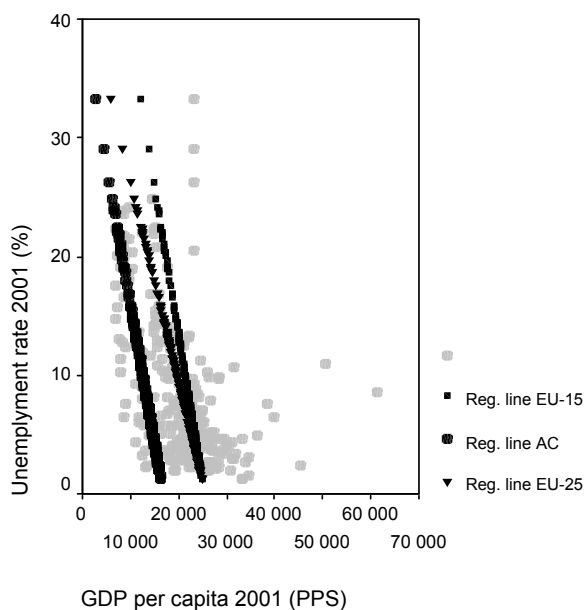


Chart 8: The regression lines of the two criteria (EU25, EU15, AC), 2001

Looking at the chart, it is quite clear that analysing the two patterns together (the regions of the 25 countries), the gradient of the regression line is distorted towards the line of the new member states. It is due to the great number of regions having high unemployment rate, but it is also to be noted that its constant value converges to that of the EU regions' line.

Okun was the first to make an analysis between GDP and the unemployment rate and created the Okun's Law. I got the following results after calculating the percentage of the GDP per capita, and that of the average yearly increase of unemployment rate<sup>6</sup>, and after illustrating the results. During the four years the majority of the regions of the 15 countries increased their GDP and decreased their unemployment rate. As for the regions of the ten countries, GDP grew but also a significant increase was seen in unemployment rate.

I received a surprising result when I examined the relation between the two modified criteria<sup>7</sup>. The test shows hardly any – rather negligible - relation between the two criteria. So in the analysed period there is no correlation (0,071; 0,109) between the average increase of the GDP per capita (PPS) (in %) and the increase of the unemployment rate (in%)<sup>8</sup>.

<sup>6</sup> I must point out that the analysed period is relatively short compared to the normal econometric analyses, but due to the lack of comparative data, a longer was not possible. The results do not provide far-reaching consequences.

<sup>7</sup> For safety reasons of the analysis I used both the Spearman and the Kendall indices.

<sup>8</sup> The values are less significant.

Chart 3: The correlation of the average change of the two criteria (EU25)

Correlations		
		Unemp. rate in %points 1998-2001
<b>Kendall's tau b</b>		
Correlation Coefficient	Mean of GDP grow in %point 1998-2001	0,071
Sig. (2-tailed)		0,096
<b>Spearman's rho</b>		
Correlation Coefficient	Mean of GDP grow in %point 1998-2001	0,109
Sig. (2-tailed)		0,083

It was obvious from the graph analysis that the relation between the two criteria is different in case of the EU-15 regions and those of the 10 new member states. It is worth examining the two patterns separately, where I also had surprising results.

Chart 4: the correlation of the average change of the two criteria (EU15, AC)

Correlations			
	EU15		AC
	Unemp. rate in %points 1998- 2001		Unemp. rate in %points 1998-2001
<b>Kendall's tau b</b>			
Correlation Coefficient	Mean of GDP grow in %point 1998-2001	-0,018	Mean of GDP grow in %point 1998-2001
Sig. (2-tailed)		0,697	0,256*
<b>Spearman's rho</b>			
Correlation Coefficient	Mean of GDP grow in %point 1998-2001	-0,031	Mean of GDP grow in %point 1998-2001
Sig. (2-tailed)		0,650	0,391*

I got similar results in EU-15 regions and in those of the 25 countries. The relation between the two criteria is very weak, almost nothing but the direction of the relation is negative (-0,11; -0,18). Nevertheless the direction of the relation in case of the 10 countries' regions is positive (!), and quite weak (0,234; 0,366). So, the higher GDP increase in a region of one of the 10 new countries, the higher the increase of the unemployment rate.

## 5. Summary of the analysis

First I analysed the regional GDP data. During the application of certain examination methods, it turned out that there are significant differences of the absolute values and of the GDP volume in EU25 regions. In the majority of the cases GDP showed growth in the period in question. At the same time, in most cases disparity grew among countries as regions having high GDP values increased their advantage while those having lower values were not able to increase their figures, it being obvious from the extreme values. As for GDP the Spanish and the Hungarian regions showed a different picture in the analysed period. There are no Spanish regions with outstanding results while in Hungary the middle part of the country is clearly the first.

When analysing the unemployment rate, bigger disparity of the observed period in EU25 countries than in case of GDP. In almost half of the countries the rate decreased during the four years and increased in several countries. There was also a country where the direction of the change was not clearly visible. There was not a region with outstanding results in case of the new member countries, but unemployment rate increased dramatically in 50% of the regions. A continuous decrease was felt in EU15, and the same regions had outstanding result during the three years.

During the analysis of the relation between GDP per capita and the unemployment rate, the direction of the closeness of the relation is negative (reverse) and that year after year it is stronger and stronger. The Spanish and the Hungarian analysis showed different results at NUTS3 level. The relation is not significant if we take the two examples together. I got the expected results though when I separated their analysis. I have found that the slope of the regression line is higher and the constant value is also higher and higher. If we take the regression line of the regions of the EU15 and the new member states, there is not a big difference between the slope of the two lines while it was significant in its constant value.

I calculated the average yearly increase of the two criteria for four years based on Okun's Law and examined the relation of the two criteria. There was no correlation between the GDP per capita and the increase of the unemployment rate in EU25 regions for the period of 1998 and 2001. Continuing the analysis, I divided the growth indices into EU15 and new member states and examined the relation between the two criteria. On a regional level, the relation between the GDP per capita and the unemployment rate of the EU15 countries in the analysed period is very weak and its direction is negative. In case of the new member states the relation is fairly weak but has a positive direction. After the analysis I drew the following conclusion: Okun's Law is not necessarily valid on a regional level. I must make further analyses to improve the regional evaluation of Okun's Law.

The regional analysis of the GDP per capita and the unemployment rate opens a new chapter among the theories of macroeconomics. It has become clear that surprising and quite different results can come out of such analyses.

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## **HUMAN ACTORS IN REALITY AND IN MODERN ECONOMIC THEORIES**

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### **1. Introduction**

A most recent definition of economics says that “economics studies how individuals, firms, government and other organisations within our society make choices and how these choices determine society’s use of its resources”<sup>1</sup>. Therefore, all economic processes are carried out by man; either by individuals or by economic actors having an institutional form like firms, governmental or other institutions. The latter employ man and all their decisions are made by them.

If we want to describe economic processes, humans are requisite actors: they have to be included in economic theories. However, the appropriate model of man in economic theories has to fulfil several requirements. Though it should be a manageable factor for economists involved in economic forecasting, at the same time it cannot be too simple through ignoring factors influencing human behaviour.

Classical economists (Adam Smith and Alfred Marshall) regarded man as he was: man with common sense, virtues, passions and emotions. With the neoclassical movement, the official language of economics became a certain type of formalized language; the model of the human economic actor was formalized as well. Modern economists (Ricardo and the neoclassical) introduced the “economic man”<sup>2</sup>, whose only aim is profit maximization and whose only virtue is prudence. Their model fulfils the requirement of applicability and simplicity. Concerning the requirement of completeness some thoughts are to be made. If we know more about man who are actors of real economy, we will have a truer picture about economy. We will have more clues to find out and understand the behaviour of economic actors if we go beyond the “economic man”. The aim of the paper is to give an overview about factors influencing human behaviour.

### **2. Man in modern economics**

When mentioning the concept of modern economics, authors usually refer to neoclassical economic theories. The methodology of these theories uses a certain type of formalized language with equations, axioms, hypotheses borrowed from mathematics and physics. If a method fits in mathematics, it should work in economics as well. For equations, manageable variables are necessary.

In a modern economic model the human actor can be either regarded as a constant quantity or a dependent variable. In the second case the number of explaining variables that determine human behaviour should be reduced in order to make the equation manageable.

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<sup>1</sup> [Stiglitz, J. E. – Walsh, C. E. 2002, p.4.]

<sup>2</sup> [Veblen, T. 1931, p. 241.]

To meet all the requirements of modern economics, neoclassical economists introduced the “homo economicus” i.e. “the economic man”, the model of human economic actors. They made preliminary assumptions like “all economic actors are rational” and “possess all information” in the competitive market. Their only aim is the maximization of their utility. Formal economists used as much simplification as possible, i.e. they reduced all human traits of man to prudence. The economic man is armed with all knowledge necessary for making a decision in order to maximize his utility and with common sense so as to use disposable information best. Above prudence, no other virtues characterise the neoclassical man. His motives were simplified to utility, i.e. no other aims are there for him except reaching the maximum level of utility by given resources or given costs; or reaching a given level of utility with the least resources or at lowest costs.

Alfred Marshall, the great economist wrote that “Ricardo and his followers neglected a large group of facts” because “they regarded man as, so to speak, a constant quantity” and did not allow for “human passions, instincts and habits”<sup>3</sup>.

All in all, the “homo economicus” is the product of the neoclassical movement and lives further in today’s modern economic theories. It fits perfectly in the modern economic methodology and is easy to handle. In the simplified theories written in a formalised language – including formulas borrowed from mathematics and physics – there is no place for a speaking man who is not a constant quantity but has non-selfish motives and emotions. All these characteristics of economic actors should be included in formalist equations as variables; however, this would make modern economic theories collapse.

### 3. Refutation of the “economic man”

#### 3.1. *Man in literary economics*

When economics was established as an independent scientific discipline, economic theories were expressed in natural language, i.e. literary economics. Economists used both facts and evaluation in their theories. They described and evaluated economic events and actors with words.

Before *The Wealth of Nations*<sup>4</sup> Adam Smith, the great classical economist wrote another famous book *The Theory of Moral Sentiments*<sup>5</sup>, about human behaviour. The 6th edition (1790) of the book is about the ethical theory of the author. A virtuous economic actor possesses not only prudence but love, courage, justice and temperance as well. The economic man does not possess these qualities.

In his famous book Alfred Marshall defines economics as “a study of mankind in the ordinary business of life<sup>6</sup>. About the interpretation of human actors in economics he states that economics deals “not with an abstract or “economic man; but a man of flesh and blood. They deal with a man who is largely influenced by egoistic motives in his business life to a great extent with reference to them; but who is also neither

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<sup>3</sup> [Marshall 1885, p.155.]

<sup>4</sup> [Smith, A. 1976]

<sup>5</sup> [Smith, A. 1982]

<sup>6</sup> [Marshall, A. 1920, p.1.]



above vanity and recklessness, nor below delight in doing his work well for its own sake, or in scarifying himself for the good of his family, his neighbours, or his country; a man who is not below the love of a virtuous life for its own sake”<sup>7</sup>.

Neither author concentrates on prudence only: although they declare the major role of common sense they do not exclude other human traits. These all should be calculated with when creating an economic theory including human actors.

### **3.2. Features of man in reality**

Thorstein Veblen in “The Theory of the Leisure Class” originally aims to illustrate the circumstances, habits and thoughts of the upper and the upper-middle class of the 19<sup>th</sup> century. However, the essence of the book is topical even today. As I read the book, I found it as the perfect refutation of the “economic man”. Almost every chapter shows other than rational motives of economic actors that would improve either one’s or the society’s well-being but compliance with prescribed canons. Belief in luck and devout observances are no prudent thoughts either. The paper aims to give an overview on all motives and beliefs that influence real economic actors but are unknown to the “economic man”.

#### *3. 2. 1. Being Honorific*

The greatest desire of man has always been and is even today to be honoured, to be reputable. For the fulfilment of these two desires they are willing to do everything: they make not only irrational decisions but forget to maximise their utility as well by spending fortunes on properties prescribed by canons.

In Maslow’s Hierarchy of Needs esteem i.e. “needs based on the attention and recognition that comes from others” can be found almost on top of the hierarchy after the three levels below (physiological, safety and love needs) have been fulfilled. For the “economic man” it would be evident to fulfil these 3 levels beginning with the physiological needs. After the fulfilment of these, esteem needs can be satisfied. The order is of strict importance.

Veblen states that in order to get self-respect and the envy of others, however unaffordable it is people are willing to run into large expenditures, which is a far cry from the “economic man”. They put esteem needs before more important needs, however inconvenient it is.

##### **3. 2. 1. 1. Gaining self-esteem**

First of all we have to find the basis of self-esteem in all ages. In barbarian cultures when there was no property, the basis of self-esteem was evidence of prowess: trophies and visible success. An invidious distinction arises between exploit and acquisition by seizure on the one hand and industrial employment on the other hand. Arms are honourable and the use of them became an honorific employment. At the same time, employment in industry becomes correspondingly dishonourable, and

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<sup>7</sup> [Marshall, A. 1920, p.22.]

labour becomes irksome. With the primitive barbarian, an honorific act referred to “a recognised successful act of aggression; and where aggression means conflict with men and beasts, the activity which comes to be especially and primarily honourable is the assertion of the strong hand”<sup>8</sup>.

Gradually, as industrial activity further displaced predatory activity in the community’s everyday life and in man’s habits of thought, accumulated replaced property more and more trophies of predatory exploit. A struggle between men for the possession of goods began. The motive that lies in the root of ownership is emulation. The possession of wealth confers honour, so the accumulation of wealth confers more honour. “Ownership began and grew into a human institution on grounds unrelated to the substance minimum”<sup>9</sup>. Property became the most easily recognised evidence of success and therefore became the conventional basis of esteem. “Its possession in some amount becomes necessary in order to any reputable standing in the community. It becomes indispensable to accumulate, to acquire property, in order to retain one’s good name. ...Prowess and exploit may still remain the basis of award of the highest popular esteem, although the possession of wealth has become the basis of common place reputability and of a blameless social standing”<sup>10</sup>. As soon as the possession of property becomes the basis of popular self-esteem it also becomes a requisite to that compliancy which we call self-respect. Wealth inherited from ancestors was the most honourable.

The desire to excel in pecuniary standing and so gain the esteem and envy of one’s fellow-men were more important motives than wealth. The wealth or power must be put in evidence, for esteem was awarded only on evidence. Relative success, tested by an invidious pecuniary comparison with other men, became the conventional end of action. “Among the motives which lead men to accumulate wealth, the primacy, both in scope and intensity, therefore, continues to belong to this motive of pecuniary emulation”<sup>11</sup>.

### 3. 2. 1. 2. Honorific employments

The “economic man” would think: if I work properly I will have money. If I work harder I will have more money. According to the principle of utility-maximisation, in a system of coordinates with axes “time at work” and “free time” I will make a rational decision so that I have enough money and enough rest.

According to Veblen the principle of “being honorific” rules in the evaluation of employments. In ancient times, there was a distinction between “exploit” and “drudgery”. Employments which are to be classed as „exploit” and result in visible success are worthy, honourable, noble; other employments which do not contain this element of exploit and do not lead to visible success, especially those which imply subservience or submission, are “unworthy, debasing and ignoble”. Similarly, persons involved in exploit are honourable; others involved in drudgery are unworthy. Therefore “esteem is gained and dispraise is avoided by putting one’s efficiency in

<sup>8</sup> [Veblen, T. 1931, p. 17.]

<sup>9</sup> [Veblen, T. 1931, p. 26.]

<sup>10</sup> [Veblen, T. 1931, p. 29.]

<sup>11</sup> [Veblen, T. 1931, p. 34.]

evidence. The result is that the instinct of workmanship works out in an emulative demonstration of force<sup>12</sup>.

In modern times, in industrial communities and under the “regime of emulation”<sup>13</sup> two other types of employment were distinguished: the “pecuniary” and the “industrial”. Pecuniary employments had to do with ownership and acquisition while industrial employments covered non-economic employments and those of production and workmanship. The first category was regarded “honorific” and was reserved for the upper-class. Some fields of honorific employments were politics, higher administration, priestly and military service. Some concrete titles of honorific positions were “the office of a Maid of Honour or of a Lady in Waiting to the Queen, or the King’s Master of the Horse or his Keeper of the Hounds”<sup>14</sup>. The common in them is that they do not have to do with productive work. A life of leisure is the readiest and most conclusive evidence of pecuniary strength representing superior force. Conspicuous abstention from labour therefore became the “conventional mark of superior pecuniary achievement” and “the conventional index of reputability”. The performance of labour on the other hand has been accepted as conventional evidence of inferior force and labour became unavoidably dishonourable as being the evidence of property. “Prescription ends by making labour not only disreputable in the eyes of the community, but morally impossible to the noble, freeborn man, and incompatible with a worthy life”<sup>15</sup>. As productive work was regarded as unworthy, non-productive consumption of time was honorific and represented “evidence of pecuniary ability to afford a life of idleness”<sup>16</sup>.

### 3. 2. 1. 3. Honorific knowledge

In ancient times it was only priests who had some kind of knowledge. Although this “was knowledge of ritual and ceremonial; that is to say, a knowledge of the most proper, most effective, or most acceptable manner of approaching and of serving the preternatural agents”<sup>17</sup>. That is why learning can be considered in some sense as a by-product of the “priestly vicarious leisure class”. This knowledge was called “higher learning” which could be practiced only by priestly classes. This knowledge had no economic or industrial effect. Another kind of knowledge appeared serving industrial purposes and turned to account for industrial services. A demarcation line between these two kinds of knowledge was observable: the former was considered as higher learning and the latter as lower learning. “Familiarity with the animistic superstitions and the exuberant truculence of the Homeric heroes” and knowledge like that was “higher”, “nobler”, “worthier” than matter-of-fact knowledge of things and a contemplation of latter-day civic or workmanlike efficiency, which was regarded “lower”, “base”, “ignoble”<sup>18</sup>.

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<sup>12</sup> [Veblen, T. 1931, p. 16.]

<sup>13</sup> [Veblen, T. 1931, p. 229.]

<sup>14</sup> [Veblen, T. 1931, p. 79.]

<sup>15</sup> [Veblen, T. 1931, p. 41.]

<sup>16</sup> [Veblen, T. 1931, p. 43.]

<sup>17</sup> [Veblen, T. 1931, p. 364.]

<sup>18</sup> [Veblen, T. 1931, p. 392.]

A certain type of knowledge, i.e. the knowledge of expensive services and articles of consumption (beverages, cheese, weapons, dances and narcotics) was honorific as well. This needed a special type of training and the special milieu of the “leisure of gentleman” where he could obtain and improve his knowledge. Certainly this came into fashion with the consumption of more excellent foods. The specialist should discriminate between “the noble and ignoble in consumable goods”<sup>19</sup> as well.

The “Maecenas-function of the well-to-do” arrived as a cultural approach, or from the interest of reputability, rather than from that of the economic interest. Scholars who performed proficiency in the classical lore and humanities were sponsored in order to have vicarious leisure. This knowledge tends to lower rather than to heighten the industrial efficiency of the community.

Reading classics was extremely honorific: first it served to shape the taste of the novices and the intellectual attitude, second, it consumed the learner’s time, which was only affordable for extremely well-off members of the community who did not need time for earning money. The knowledge of classics was of economically disserviceable kind and it was evidence of wasted time and pecuniary strength. The knowledge of ancient languages and elegant diction both reading and writing are effective means of reputability. “Elegant diction” is “archaic, cumbrous, and ineffective; its acquisition consumes much time and effort; failure to acquire it is easy of detection. Therefore it is the first and readiest test of reputability in learning, and conformity to its ritual is indispensable to a blameless scholastic life”<sup>20</sup>.

### 3. 2. 1. 4. Non-individual interests

As the economic man is selfish he is unimaginable to act with the consideration of non-individual interests. The analysis of our everyday life shows that quite a large number of human actions is done by non-individual motives.

Among non-individual motives the motives of charity and of social good-fellowship, or conviviality; or, in more general terms, the various expressions of the sense of human solidarity and sympathy and the “sense of aesthetic congruity” with the environment can be mentioned. “This non-invidious residue of the religious life -- the sense of communion with the environment, or with the generic life process -- as well as the impulse of charity or of sociability, act in a pervasive way to shape men’s habits of thought for the economic purpose”<sup>21</sup>. Organisations with other than invidious purpose in life appeared. Their purpose is some work of charity or social amelioration. These organizations are often of a quasi-religious or pseudo-religious character, like the agitation for prison reform, for the spread of education, for the avoidance of war by arbitration or for disarmament. University settlements, neighbourhood guilds, sewing-clubs, art clubs, and even commercial clubs, and, in some light measure the pecuniary foundations of semi-public establishments for charity, education, or amusement are of the same character. At first glance, these actions seem like wonderful movements for the amelioration of the situation of the

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<sup>19</sup> [Veblen, T. 1931, p. 74.]

<sup>20</sup> [Veblen, T. 1931, p. 399.]

<sup>21</sup> [Veblen, T. 1931, p. 334.]

poor. For second glance, beyond these unselfish actions the desires for reputability and honour can be discovered. "These (establishments) serve to authenticate the pecuniary reputability of their members, as well as gratefully to keep them in mind of their superior status by pointing the contrast between themselves and the lower-lying humanity in whom the work of amelioration is to be wrought; as, for example, the university settlement, which now has some vogue"<sup>22</sup>. Where there is a devout colouring present it lowers the immediate efficiency of the organizations for any economic end to which their efforts may be directed. Many organizations, charitable and ameliorative, divide their attention between the devotional and the secular well-being of the people whose interests they aim to further. It can scarcely be doubted that if they were to give an equally serious attention and effort undivided to the secular interests of these people, the immediate economic value of their work should be appreciably higher than it is. In reality, the solicitude of settlements is in part directed to enhance the industrial efficiency of the poor and to teach them the more adequate utilization of the means at hand.

The propaganda of culture can be related to this topic. Reputability under the guidance of the leisure-class formulation of the principles of status and pecuniary decency, and consequently the success of the individual is to a great extent dependent on his proficiency in demeanour and methods of consumption that argue habitual waste of time and goods, therefore, social good repute will be ultimately reducible to terms of pecuniary merit<sup>23</sup>. That is why it would suit no one to have the enterprise conducted with a view directly to the most economical and effective use of the means at hand for the initial, material end of the foundation without presenting a large number of expensive decorum, as "some considerable share of the expenditure should go to the higher or spiritual needs"<sup>24</sup>.

### 3. 2. 2. *Utility*

#### 3. 2. 2.1. Utility of servants

The economic man would think the following: "If I have work which could be done perfectly by 6 persons, I am not willing to employ the 7th one for the same work. It would not be rentable. I am looking for the most effective servants within a given budget constraint or I am looking for the cheapest servants available. My aim is to reach the work to be done properly at the lowest cost. I will not keep many servants for show only some that are unavoidable."

How did the question look like for a well-to do real man? He valued women and other slaves highly, both as evidence of wealth and as a means of accumulating wealth. Not for their services but for show. Their number was not a question of efficiency but of the master's ability and willingness to pay. As the accepted evidence of wealth is the possession of many women, and presently also of other slaves engaged in attendance on their master's person and in producing goods for him. That

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<sup>22</sup> [Veblen, T. 1931, p. 341.]

<sup>23</sup> [Veblen, T. 1931, p. 345.]

<sup>24</sup> [Veblen, T. 1931, p. 350.]

is why a special class of personal or body servants was of very grave importance. These specialised servants are useful more for show than for service actually performed. Actually, they were to serve as a means of good repute rather than as a means of comfort and their service was of ceremonial character, in other words, for the performance of “conspicuous leisure”. As Veblen states “the utility of these comes to consist, in great part, in their conspicuous exemption from productive labour and in the evidence which this exemption affords of their master’s wealth and power”<sup>25</sup>.

There is another component of the servant’s utility: the aptitude and acquired skill in the formal manifestation of the servile relation. The servant has to be aware of his place: the leisure of the master is his own but the leisure of the servant is the leisure of the master. This is true for highly paid servants, as well as one for the chief ornaments of the well-bred housewife.

Special training in personal service costs time and effort. “So that trained service has utility, not only as gratifying the master’s instinctive liking for good and skilful workmanship and his propensity for conspicuous dominance over those whose lives are subservient to his own, but it has utility also as putting in evidence a much larger consumption of human service than would be shown by the mere present conspicuous leisure performed by an untrained person”<sup>26</sup>. To sum up the chief use of servants is the evidence they afford of the master’s ability to pay.

### 3. 2. 2. .2. Utility of goods

The economic man would define the utility of things in the following way: “utility means all the useful features of a good and the feeling of satisfaction derivable from the consumption of the good”. It is pure efficiency that counts, i.e. the proportion of fulfilling the task the good is designed for. The beauty and aesthetic value of goods would mean economic value and serviceability first, beauty next. The price of goods would be in direct proportion with their industrial serviceability.

Actually canons of reputability have effect upon the popular sense of beauty or serviceability in consumable goods. The requirements of pecuniary decency have influenced the sense of beauty and of utility in articles of use or beauty to a very appreciable extent. Articles are to an extent preferred for use on account of their being conspicuously wasteful; they are felt to be serviceable somewhat in proportion as they are wasteful and ill adapted to their ostensible use.

The utility of articles valued for their beauty depends closely upon the expensiveness of the articles. For serviceable goods, it is not only brute efficiency that counts. Our higher appreciation of the superior article is an appreciation of its superior honorific character not the appreciation of its real beauty although the requirement of conspicuous wastefulness is not consciously present in our canons of taste. Precious stones, metals and some other materials used for adornment and decoration owe their utility as items of conspicuous waste to an antecedent utility as objects of beauty. The more gold is used for the decoration of some piece of art, the more beautiful it is regarded however poor the quality of the handwork is. “The utility

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<sup>25</sup> [Veblen, T. 1931, p. 55.]

<sup>26</sup> [Veblen, T. 1931, p. 61.]

of these things to the possessor is commonly due less to their intrinsic beauty than to the honour which their possession and consumption confers"<sup>27</sup>.

If an object is considered valuable, it has to fulfil two requirements at the same time: both the requirement of beauty and expensiveness. The marks of expensiveness mean the beautiful features of expensive articles. If the article does not pass the requirement of expensiveness, no matter how a sophisticated handwork it is, it cannot be regarded as beautiful. Although pecuniary beauty was supplemented by aesthetic beauty, the canon of expensiveness (as a waste of money) is still considerable.

Goods are not only bought for consumption necessary for the subsistence minimum but for accumulation. The "emulative propensity" of man motivates people for further accumulation of goods: not only useful but rare and expensive goods. Later on Veblen states that the "aggregate serviceability" i.e. the utility of a good consists of two elements: "a honorific element" together with "the element of brute efficiency"<sup>28</sup>. The honorific element can be derived from the costliness of expensive goods. The high price meant a "secondary utility" serving to demonstrate the buyer's ability to pay. Consuming such expensive goods became "meritorious" and the consumption of inexpensive goods was regarded dishonourable because such goods were "cheap and nasty"<sup>29</sup>.

The "honorific element" in goods is not only a requirement for consumers but for producers as well. Producers have to alter their production methods so as to produce more sophisticated products and use more exclusive and rare materials. The production process should take a very long period, i.e. it should be a waste of time. If the production process fulfils these requirements, goods can be sold at high price as the honorific element of goods will be discovered by costumers and those will be glad to buy such articles in order to show their "pecuniary strength".

As hand labour is a more wasteful method of production, marks of hand labour are honorific. Machine-made products are regarded as common goods, their consumption is not honorific. These are cheap while hand-made products are expensive; the imperfection on workmanship on them is visible. The same concerns especially the book-making industry: more elegant books are printed only in limited editions in old-style on laid pare and with uncut edges. These hand-made books are more expensive and less convenient for use than books turned out with a view to serviceability alone. These books are superior to machine-printed products.

Animals serving for no industrial end such as pigeons, parrots and other cage-birds, cats, dogs and fast horses are really expensive. They have no economic utility but have the secondary utility; that is why they are regarded as honorific. They are means of conspicuous leisure and evidence of wasted time and money. Domestic animals like angora cat, which are honorific, are reputed beautiful.

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<sup>27</sup> [Veblen, T. 1931, p. 129.]

<sup>28</sup> [Veblen, T. 1931, p. 157.]

<sup>29</sup> [Veblen, T. 1931, p. 155.]

### 3. 2. 3. *Canons of taste*

We have to begin with a correct answer to the following question: „What factors determine the bundle of goods actually bought by the consumer?” These are consumer preferences that are different for individuals. For the “economic man”, the best combination of goods is the one that is affordable by his budget constraint and is situated on his highest utility curve at the same time. For him, there are no prescribed rules of taste, no canons, which he has to fulfil.

According to Veblen one of the main rules influencing individual consumption is the canon of “reputability”. In order to be „reputable and honorific, one has to consume the most expensive and rare goods of best quality. The “leisure of gentleman” should follow this rule. However, not everything is allowed for everyone: the consumption of luxurious goods and exclusive food was “tabu” for children and woman<sup>30</sup>. Certain beverages, articles of food and narcotics were reserved for the most well-off. As these articles were allowed only for a small community, consequently, their consumption was honorific. Some diseases derivable from the consumption of some strong beverages and narcotics were considered honorific as well, as evidences of “gentle blood” and “well-breading”. On the other hand men who could not allow consuming the best quality of food were regarded as “ignoble”. The consumption of mass product was the evidence of “inferior force and demerit”<sup>31</sup>.

As the life of the upper-class was continuously under vigilant eyes, the gents of leisure had to consume for show. The best way of that was the above mentioned consumption of high quality food in huge quantity, because they were extremely expensive. The larger quantity consumed represented a larger waste of money and therefore it was honorific. Another way of putting one’s pecuniary strength in evidence was to give valuable gifts like precious stones or works of art containing as much gold as possible. Similarly, the main aim of giving balls and feasts was not to make a vivid party for the lowest possible cost and resources but to demonstrate one’s ability to pay to the invited and make them feel envy.

#### 3. 2. 3. 1. *About dresses and costumes*

The best expression of “reputability” could be seen in dresses and costumes. It was a well-known statement that “a cheap coat makes a cheap man”<sup>32</sup>. Therefore, the more a dress costs, the more beautiful we find it. Wearing expensive dresses is the best way to put in evidence pecuniary success and social worth. These pieces show that the wearer can consume freely and uneconomically, and he is not engaged in any kind of productive work. A dress should not only be expensive: it should be spotless as well in order to demonstrate the wearer’s abstinence from any productive employment. “The native dignity of a gentleman” could be supported by special pieces like patent-leather shoes, stainless linen, lustrous cylindrical hat and a walking-stick which made work impossible for the wearer<sup>33</sup>.

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<sup>30</sup> [Veblen, T. 1931, p. 69.]

<sup>31</sup> [Veblen, T. 1931, p. 74.]

<sup>32</sup> [Veblen, T. 1931, p. 156.]

<sup>33</sup> [Veblen, T. 1931, p. 171.]



Another important feature is that dress should be not only conspicuously expensive and inconvenient; it must be up to date at the same time. As fashion changes from season to season, each garment is permitted to serve only for a brief term. The new style must conform to the requirement of “reputable wastefulness” and “futility”. Naturally it should testify the wearer’s exemption from or incapacity for all vulgarly productive employment.

Dress designers who prepared dresses for upper-class women, used such techniques that caused the wearer special pains making her look totally vulnerable and incapable of any kind of productive work. As far as feminine beauty is concerned, the ideal was not designed under the surveillance of physiological wellbeing. Women were merely regarded as a means of good repute, “the ideal (woman) requires delicate and diminutive bands and feet and a slender waist”. Requirements for women like “constricted waist” in Western cultures and also “the deformed foot of the Chinese”<sup>34</sup> were welcomed by men and the “resulting artificially induced pathological features” were regarded attractive as well. As these alterations took enormous time, effort and were compulsory mainly for well-bred women, they were regarded extremely honorific. At the same time, they made women expensive, useless for any kind of productive work and dependent largely on their master. “In concrete terms: the high heel, the skirt, the impracticable bonnet, the corset, and the general disregard of the wearer’s comfort which is an obvious feature of all civilized women’s apparel, are so many items of evidence to the effect that in the modern civilized scheme of life the woman is still, in theory, the economic dependent of the man”<sup>35</sup>.

Consequently women did not wear such inconvenient but luxurious dresses and expensive jewellery for their own sake but for their master’s, in order to make show for others’ vigilant and jealous eyes. Sadly, the sole economic function of woman is to put in evidence the household’s ability to pay.

A special kind of fashion could be observed in uniforms of dependents. These uniforms expressed servitude. Uniforms of some honorific employees like “Maid of Honor or of a Lady in Waiting to the Queen, the King’s Master of the Horse or his Keeper of the Hounds”<sup>36</sup> were elegant, spotless and made of expensive materials. These uniforms were not comfortable or serviceable for fulfilling the task, either. The nicer and costlier they were, the greatest the honour of the master was.

A third type of robes is costumes of priestly employees. “Devout consumption” is similar to “vicarious leisure” as the leisure of priestly employees is not their own. Whatever they do, they do it for the glory of God. Whatever they are wearing they do it for the glory of God or of an “anthropomorphic divinity”. The budget of their costumes is not guided by rational reasons: the “priestly vestments” are “notoriously expensive”, uncomfortable and spotless. Their material was expensive, their design looked “honorific” and the garments of priestly principals were ornated with precious stones. These vestments were clear evidence of the master’s ability to pay. These costumes were worn not only at ceremonies but on countless rehearsals as well. The immaculate appearance of priests was a requirement to give honour before a divinity

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<sup>34</sup> [Veblen, T. 1931, p. 149.]

<sup>35</sup> [Veblen, T. 1931, p. 182.]

<sup>36</sup> [Veblen, T. 1931, p. 79.]

and to show other people their superiority. Priests had not only to take care of their garments and their physical appearance; they were not allowed to have their hands worn or their nails dirty, either. Consequently, for priests abstinence from vulgarly productive work was compulsory.

### 3. 2. 4. *Habits and Tradition*

In point of reputability it was the “leisure class” standing at the head of the social structure. As each class envied the class next above the social scale, it was the upper class who set up standards of living that served as a pattern to be followed for each class below. These standards not only influenced the habits of consumption but habits of thought and behaviour as well. In a middle class family while the wife showed a life of leisure her husband was working in order to earn the amount of money necessary for representing the affordable highest level of leisure.

The requirements of joining the leisure class differed from time to time. In the early barbarian, “the test of fitness was prowess” and the ideal candidate was “gifted with clannishness, massiveness, ferocity, unscrupulousness, and tenacity of purpose”<sup>37</sup>. These features enabled him to the accumulation of wealth. Later on, the entrance requirement had changed to the “possession of wealth”. The ideal “pecuniary man” ignored the feelings and regards of others and he was unscrupulous in his actions. “The aristocratic and the bourgeois virtues -- that is to say the destructive and pecuniary traits -- should be found chiefly among the upper classes, and the industrial virtues -- that is to say the peaceable traits -- chiefly among the classes given to mechanical industry”<sup>38</sup>.

We do not have to forget the requirement of gentility. Gentility could be seen in the degree of proficiency in one’s manners, tastes and habits of life. As good breeding requires time and energy, the higher proficiency one shows in these features, the more time he has wasted and until that period it is evident that he was not involved in vulgarly productive work. The “code of status” requires absence from any kind of productive work.

As the classes below made efforts to follow the habits of life of the more-well-off, their descendants received these habits as their own. Once the canons of “conspicuous consumption” and “conspicuous leisure” are habituated, the next generation will take it natural and will not remember their original habit of living. Besides “inherited aptitudes”, “transmitted aptitudes”<sup>39</sup> i.e. features of the dominant ethnic element of a community are dominant in determining the everyday habits of a community.

As the life of the well-off is always in the focus of attention, the “propensity for emulation”<sup>40</sup> will result in visible evidences. Emulation of “honorific expenditures”<sup>41</sup> and conspicuous consumption will be demonstrated in most eye-catching ways.

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<sup>37</sup> [Veblen, T. 1931, p. 236.]

<sup>38</sup> [Veblen, T. 1931, p. 241.]

<sup>39</sup> [Veblen, T. 1931, p. 108.]

<sup>40</sup> [Veblen, T. 1931, p. 110.]

<sup>41</sup> [Veblen, T. 1931, p. 117.]

It is important to notice that changes in the environment or in economic needs do not affect the upper-class. They are in a sheltered position from starvation; they do not have to adopt themselves to the changed working conditions caused by the industrial revolution. Their interest is to maintain the prevailing situation. This insistence to the prevailing conditions is called conservatism. As conservatism was only a feature of the well-off members of community, it was regarded “decorous” and “honorific”.

Contrary to conservatism, innovation was the feature of the working-class; consequently it was considered “vulgar”<sup>42</sup>. It was not so easy to support innovation as certain mental efforts and energy surplus were necessary. Members of the upper-class were unwilling to spend time and dedicate thoughts on innovation, therefore they supported conservatism. They had only pecuniary relationship with innovation, when the acquisition of factories was on schedule. Their aim was exploiting, not production. Poorest members of society (quite a wide layer) were unable to spend time on innovation as they went to earn their living all the time it was possible in order to reach or maintain the subsistence minimum and do not die from starvation. Consequently, workers were conservative as well due to lack of free capacities. These are the reasons for the “general conservative attitude”<sup>43</sup> of society.

The difference between collective and individual interests is worth discussing as well. The success of a community roots in industrial efficiency, where “honesty, diligence, peacefulness, good-will, an absence of self-seeking, and habitual recognition and apprehension of causal sequence”<sup>44</sup> are required. Contrary to these, the interest of the individual lies elsewhere. The author suggests individuals “shrewd trading and unscrupulous management” It is not so difficult to see that the interest of society is not always the same as that of the individual. The individual aptitudes are a hindrance to society, especially under the “regime of emulation”<sup>45</sup>.

### 3. 2. 5. *Archaic traits and beliefs*

As war is honourable, warlike prowess is eminently honorific in the eyes of the generality of men. The enthusiasm for war and the “predatory temper” prevailed in the largest measure among the upper classes, especially among the hereditary leisure class. “Sports shade off from the basis of hostile combat, through skill, to cunning and chicanery, without its being possible to draw a line at any point”<sup>46</sup>. Sports reflect the “attitude of emulative ferocity” with a view to gaining repute for prowess. Prize-fights, bull-fights, athletics, shooting, angling, yachting, and games of skill show all the elements of exploit and ferocity. At the same time, the canons of decorum appear in sports as expressions of a peculiarly blameless life. Ulterior wastefulness and proximate purposefulness are through a traditional and habitual mode of “decorous recreation”.

“A rehabilitation of the early barbarian temperament is exotic ferocity and cunning. Prowess manifests itself in two main directions -- force and fraud. In varying

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<sup>42</sup> [Veblen, T. 1931, p. 200.]

<sup>43</sup> [Veblen, T. 1931, p. 209.]

<sup>44</sup> [Veblen, T. 1931, p. 227.]

<sup>45</sup> [Veblen, T. 1931, p. 229.]

<sup>46</sup> [Veblen, T. 1931, p. 253.]

degrees these two forms of expression are similarly present in modern warfare, in the pecuniary occupations, and in sports and games<sup>47</sup>. These aptitudes are cultivated and strengthened by the life of sport as well as by the more serious forms of emulative life. Strategy or cunning are usual elements of games. The aptitude for fraud and astuteness in any guise and under any legitimation of law or custom, are expressions of a narrowly self-regarding habit of mind. These characteristics can be classified under the traits of the “economic man”, as his selfish motives may require the application of them. “Both are highly serviceable for individual expediency in a life looking to invidious success. Both also have a high aesthetic value. Both are fostered by the pecuniary culture. But both alike are of no use for the purposes of the collective life<sup>48</sup>”.

The “gambling propensity<sup>49</sup>” can be related to sportsmanship. Among the traits of the economic man this feature is not to be found. Gambling propensity is based on belief in luck, which has a measurable economic value. Almost every sportsman wears talismans before or during their performance. Gambling serves for the glorification of the winner as well; it is usually offered by the stronger side. He wants not only to be the winner of the event but wants a pecuniary gain as well. He desires not only the natural defeat of the rival but to cause him pecuniary loss as well. Betting is hindrance for an industrial community. This belief in luck later developed to a belief in a supernatural agent. The belief in an “anthropomorphic divinity” led to the lowering of one’s industrial intelligence. This “anthropomorphic cult” influenced one’s speed for reacting, urgency and immediacy in handling the facts of reality.

The influence of beliefs in an anthropomorphic divinity on economy can be measured in concrete numbers. In order to please the divinity, the decoration of temples and priestly vestments with precious stones and the application of expensive materials was a basic requirement. “Whether therefore ye eat, or drink, or whatsoever ye do, do all to the glory of God<sup>50</sup>”. The aim was to perform leisure for the master and the divinity not the comfort and happiness of those performing it. The objects of “devout consumption”, decoration and spotless garments did not serve any industrial end directly. As they cost a fortune, they were evidence of “conspicuous waste”. Besides women and children, according to the general rule, classes that are low in economic efficiency or in intelligence were devout. This anthropomorphic cult preserved the status of the well-off. As the artisan class lived from the money earned by their own hands, the presence of an anthropomorphic divinity was out of question for them. When they completed their task, the work was done. When not, there was no supernatural agent to do the work instead of them.

The roots of sacred holidays lie in the glorification of a divinity. On such days, it was not allowed to do vulgarly productive work and make hands dirty. The absence from work and the performance of leisure was a basic requirement on Holy Days, in order to please the divinity.

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<sup>47</sup> [Veblen, T. 1931, p. 273.]

<sup>48</sup> [Veblen, T. 1931, p. 275.]

<sup>49</sup> [Veblen, T. 1931, p. 276.]

<sup>50</sup> [Veblen, T. 1931, p. 312.]

#### 4. Conclusion

After having compared the “economic man” and the “man of flesh and blood”, we will arrive at the conclusion that the “economic man” is a more developed version of the “pecuniary man”<sup>51</sup>. As the aim of the “pecuniary man” is to maximize his wealth and property, and to be the winner of the emulation, this feature could be projected to the “economic man” when he is maximizing his utility. The “economic man” wants to win the battle between consumers and producers, he wants to buy at the lowest possible price or the best bundle of goods at a given price level. However, the “economic man” has a budget constraint. For the “pecuniary man”, there is no real budget constraint. His aim is to accumulate more evidence of pecuniary strength and to be employed in a pecuniary position which has to do with acquisition. Neither categories bother about the interests of others.

The “economic man” is a very good mean in neoclassic theories. It helps to have an overview about processes as it is better to understand a simple equation than to be lost in details. The question is whether it is worth ignoring tastes, behaviour, habits of thought and prescribed canons in order to have a manageable model. A large piece of the cake of real economy can be easily lost this way. Shall we have a true picture about real economy by applying the “economic man?” What is the relation of the predicted information gained with the help of economic models applying the “economic man” and the amount of information about human beings acting in the economy lost by applying him? Answering these questions will be a great challenge for today’s economists supporting both sides.

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<sup>51</sup> [Veblen, T. 1931, p. 238. ]



## **THE CRITISM OF THE POSITIVIST RECOGNITION WAY IN ECONOMICS**

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*At the beginning of the 20<sup>th</sup> century the applied and the theoretical economics approves the position method in physics. We might notice that for this reason the world economics is at the edge of the collapse.*

*After introducing the steps of the positivist recognition we deal with the stage of recognition and we pay attention to those standpoints that are not positivist because of their nature. This criticism formulated by this method calls our attention to the fact that the deficiency in methodology might lead to fatal misunderstanding.*

### **The steps of the positivist recognition:**

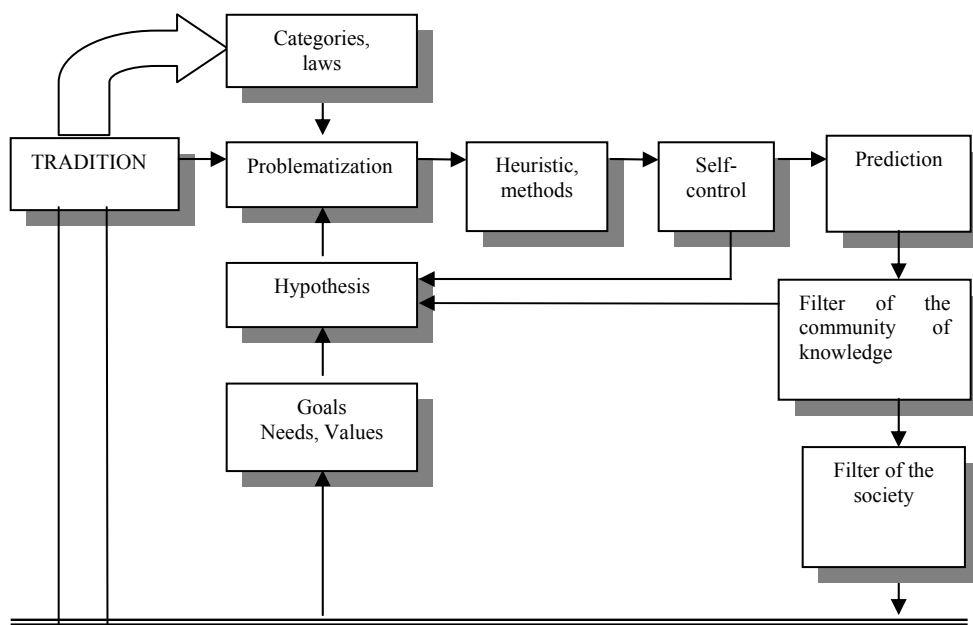
- First:* scientist or groups of scientist (as they are people) carry purposes and needs
- Second:* the scientists create a hypothesis
- Third:* they add the data, facts, knowledges made by measurement, operationalized concepts to justify the hypothesis. This step is so called problematization.
- Fouth:* the problematization will bring together those categories and laws that are essential and evident for the analysis.
- Fifth:* the laws categories and the knowledge always hides the culture based on the tradition
- Sixth:* the knowledge collected in problematization cry for order. There are mathematical, statistical explaining methods to justify the hypothesis
- Seventh:* the given data must be examined by pre-valuation. This must be opposed to the hypothesis. This means self-control.
- Eight:* The hypothesis examined by self-control makes a form of prediction. This is a statement that can lead us to valuable knowledge of the future and the reality. – says positivist scientist.
- Nineth:* The predictions published in books, newspapers are accepted firstly by the community of knowledge, they check the reality of the hypothesis.
- Tenth:* This is not a step of scientific recognition but is important in connection with the legitimization of the scientific evidence – the society approves the scientific result. ( Figure 1.)

Before giving the criticism of the positive way of recognition we pay attention for the fact that in some of the steps being exact can hardly be reached. Before this, let us to divide the sciences. There are:

- development and goal research, or
- theoretical or basic research.

The former leads to result in brevity of time, the latter makes the growth of human knowledge more important. In real, the destiny of it is the same as that of the development or goal, because the development research prepares the frame for the

applied or goal researches. The division is really important because the development and the goal research suggests that it is not value-neutral, so we must not consider it a positive science although it shows some characteristic features of the positivist recognition.



THE CHAOS OF THE REALITY  
Figure 1 Ten steps of the positivist recognition

### The criticism of the steps of the positive recognition

The logical positivism must be exact and controllable. We pay attention to the fact that it is not possible to be exact and controllable on the details of economical researches.

*First step:* the scientist of our age does not state his goals according to his values. The lack of knowledge is institutionalized. The biggest part of the scientific research is connected with interest, the other part might be considered as lacking expectation of power but one can hardly suspect the value-neutralism. Each scientist and each person expresses his goals, deeds considering own interest, so value-neutral research does not exist. In the values there are several aspects, truth and the statement of the chief-truth is a phenomenon of the society, thus it is not exact.

*Second step:* the hypothesis is based on intuition and connected to a subject. A research that does not carry the characteristics of a subject (motivation, etc.) is non existable. About the physiology of the born of the intuition it is said that is not exact.



*Third step:* the subject is extremely defenceless of its senses. It is measured by money, so the measured phenomenon is not exact. Failures move between 30-40 percent which is general. W. Heisenberg said thinking back of a journey and meanwhile washing up the dishes informed N. Bohr of the followings: “washing up is like the language. Our water is dirty, our cloth is also, but we are still able to clean the dishes and glasses. This is true for the language: we work with not clear concepts and we use a logic that is not really known but in spite of these we hope to make clearness in understanding the nature.”<sup>1</sup>

*Fourth step:* from the culture we shift the categories, laws closely in connection with the hypothesis. Although their past suggests that they were of a great use and met the requirements of being exact, but this is not acceptable for the future. We do not know eternal categories, laws but God which is the subject of belief.

*Fifth step:* a valuable problem-circle in economics has not to be divided from the everyday life, the culture, traditions, myths. This questions the seriousness of positivism.

*Sixth step:* it is hardly possible to experiment in connection with the economic phenomena, if it is possible the mentioned exact troubles certainly are made. Without experiments the economical epistemology has to look for new methods. For example thought-experiments (verbal, quantitative, qualitative, simulated experiments), evolutionary economics, describing and explained theory based on hermeneutic. These methods of heuristic have their own however in certain part of questions focus on exact and controlling idea of positivism. The above mentioned heuristical techniques are applied to one of the periods of the cognitive way, in fact the situation is inverse; the positivism is the subclass of the hermeneutic, of the evolutionary economics, a describing and explained theories, and of the thought-experiments.

*Seventh step:* the researcher compares the hypothesis with the received result. We have to decide: 1. the hypothesis is confirmed, 2. focus on the received result is rejected, 3. we rewrite the hypothesis or/and follow again the way of search. If the hypothesis is admitted we may believe that we reach the positive “truth”. If the hypothesis is not admitted in this case, the researcher confesses to be wrong along the way of exact, and he abides by his hypothesis - in this case he can start his work from the starting point -, or he rejects the hypothesis or conforms to his received results. In the economics it is not a rare occurrence to frame the dates into the hypothesis.

*Eighth step:* Making the prediction public and the legitimation of the describing and explained work are needed to be organized. The clashes of the medium (e.g. books, magazines, internet, conferences) rather discourage than advance the formation of the “clear thought”.

*Ninth step:* After processing the scientific result, the scientists decide whether the result is accurate or not. 1. According to the logical positivists if the prediction is exact in all of its elements, and the received result can be controlled, then we get at the truth, 2. According to the falsific and verifical theory if any elements of the prediction are proved that they are wrong in this case the hypothesis is exploded. If it is not proved, the received result will be acknowledged, if we know

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<sup>1</sup> Heisenberg, W. (1918): *A rész és egész*. Gondolat Könyvkiadó, Budapest, 1978.

that it contains the truth which is in the limits of the present epistemology. Th. S. Kuhn's theory of paradigm abandon the confidence of the whole truth, he argues that the "truth" of the science is a social-psychological phenomenon alone. The question is which hypothesis, theory are accepted by the knowledge society. If the basic theory helps in the concrete problems it will be true.

*Tenth step:* In fact the utility of the scientific results is not a positivistic phenomenon, instead it is a clash of the social groups in economy and in policy. The problem is that the theories and the methods advance the positivistic idea.

## Conclusion

If the exact and the controlling are queried along any points of the positive cognitive way, the positive cognition can't be continued. Focus on any steps of the ten cognitive elements we can say that it is a wrong way to speak about the positivism in economics. So the question is arised: Is it possible to improve the ecological catastrophe by the scientific method which contains many clashes? Is it possible to improve the wrong by wrong? The answer is: It is possible at random.

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## **THE IMPACT OF AGRICULTURE DEVELOPMENT ON THE REGIONAL DEVELOPMENT OF NORTHERN HUNGARY**

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### *Summary*

*The development level of regions is traditionally closely related to the capacity and competitiveness of agriculture. The region of Northern Hungary has been ranked among the most backward regions of Hungary for a long time. Although the ratio of the employed in agriculture belonging to the primary sector was the second lowest after the region of Central Hungary in 2003, the economic situation of the region is considerably influenced by its agricultural performance. The new development programs for agriculture and regional development offer a good opportunity for the agriculture of the region to develop and to decrease its underdevelopment.*

### **Measuring the regional differences within the region**

The first step of any investigation of development possibilities has to be the exploration of the regional inequalities of the region under examination. This raises the following questions: how big are the regional differences in a given area; how do they change (do they show an increase or a decrease, i.e. differentiation or equalisation is the typical tendency).

The processes of regional economic development lend themselves to an approach by a combination of two elements - growth and structural changes - , i.e. a process of creating new qualities. Both development and growth represent certain changes: in growth it is measures, and in development it is values that change.

The importance of the following factors is to be highlighted when beginning the examination:

- the multi-dimensional character of regional inequalities,
- the manifold possibilities of measurement and quantification within the individual dimensions (multi-indicator character),
- the use of regional inequality indicators with different contents,
- the relative freedom of interpreting and evaluating the results.

*Indicators* are in general numbers used for observing processes, in our case for observing social-regional processes. (Andorka,1997.) (1)

The general requirements set for them are that they should be:

- measurable,
- grasping the characteristics of the processes,
- suitable for comparison in time,

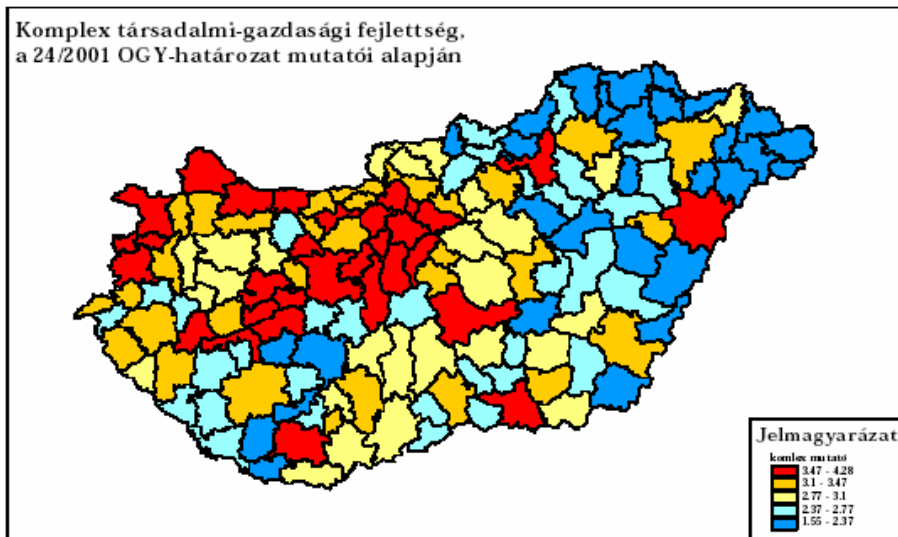
- forming a structured system and embedded into the whole of the strategy targeted,
- related to policy analyses and evaluations.

The indicators currently used in relation to agriculture in the Hungarian literature are as follows:

- share in the GDP (1 county's GDP=100%),
- regional distribution of the gross added value of agriculture (%),
- rate of production by small farmers in the added value of agriculture (%),
- gross added value of agriculture (M Ft),
- agricultural land by regions and by cultivation sector (ha),
- supply of funds/assets,
- average yield,
- live stock,
- number of agricultural organisations,
- number of one-man agricultural businesses per 1000 inhabitants,
- numbers of agricultural cooperatives, fishery cooperatives, agricultural specialist cooperatives, and smallholders,
- share of full-time producers in the registered arable land (%),
- regional distribution of large, small and medium-sized businesses (%),
- rate of farms smaller than 20 ha (%),
- average size of lands above 1000 ha of arable land,
- rate of agricultural businesses planning medium-range expansion for the following year (%).

One of the most frequently used types is the region or settlement lagging behind in social and economic terms defined in line with the complex indicators. In describing social and economic development, major importance is attributed to indicators describing the demographic and employment situation, the development level of settlement infrastructure, and that of the economy through the role of businesses. On the other hand, indicators of education and qualification have no or hardly any role, which is related to the fact that these indicators can only be measured at census. This complex indicator includes agriculture also through three indicators when defining regions lagging behind in social and economic terms:

- urbanity/rurality index (demographic indicator),
- rate of gainfully employed persons in agriculture (employment indicator),
- number of one-man businesses in agriculture per 1000 inhabitants (economic indicator).



Source: VÁTI Kht., 2002. (2)

Figure 1. Complex social-economic development, based on decision No. 24/2001 of the Parliament

For the purpose of elaborating such a complex indicator for Hungary, which is designed to illustrate the differences in regional development, more indicators of an agricultural/rural nature are needed, for more than half of the small regions of the country are of a rural character, and the rate of people making a living from agriculture is still very high.

In addition, the European Union is paying increasing attention to and spending more and more funds on making rural areas convergent and on reviving them. The European Charter of Rural Areas published by the Council of Europe in 1994 envisages a multi-function agriculture which plays a role not only in production, but also has the task to maintain the countryside and traditional culture for tourism, which is becoming more and more lively, and is of great significance in maintaining rural values, culture, and communities as well as in the performance of social tasks.

### ***Competitiveness instead of convergence***

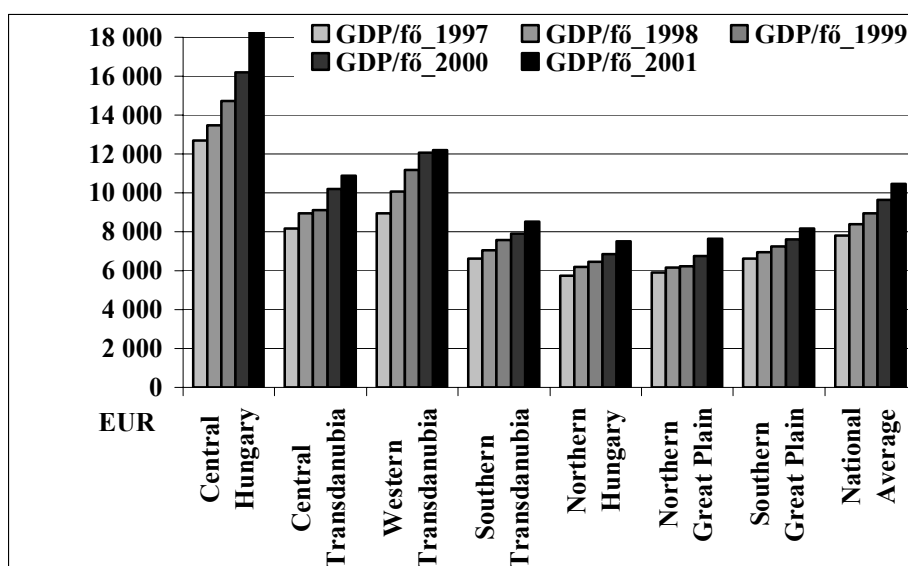
In the past years competitiveness and regional competitiveness have become one of the central issues in the European Union and its member countries. In line with the sixth regional report (1999) and the second cohesion report (2001) of the EU as well as several OECD documents, the uniform concept of competitiveness is as follows: the capability of companies, industries, regions, nations and regions encompassing nations of creating relatively high income and relatively high employment levels, while they are exposed to international (global) competition.

If competitiveness is examined at the regional level, regions, towns and countries are competitive if their economies are open and the per capita income is high and

increasing in the long run and the employment rate is of a high level and not decreasing, i.e. large ranges of the population can expect to share this income.

A paper, *Benchmarking the Competitiveness of European Industry*<sup>1</sup>, written in 1996, examines and systemises the economic conditions for improving competitiveness. The paper employs a sector approach, but its range of thought and methodology can also be adopted for regions. The model outlined is flexible, and thus can be employed for national, regional and small region levels as well: the point is that the labour market should be approximately homogeneous regionally. The paper reveals that employment and productivity are the two most important indicators of competitiveness at the level of economy. (2)

In the Hungarian regions these two indicators show great discrepancies. Central Hungary is obviously separated through its exceedingly high value and can be seen to be increasing its advantage over the other regions. Northern Hungary and the Northern Great Plain have shown a growth of negligible extent for years now.



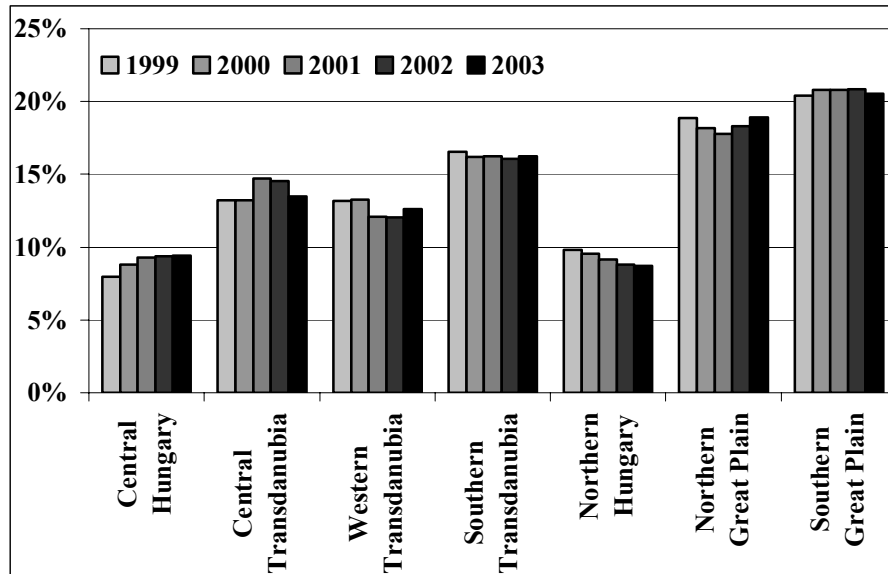
Source: Regional Statistical Yearbook, 1999-2003.

Figure 2. Per capita GDP in the regions of Hungary

The per capita gross domestic product in 1998-2002 was only 68-66-64-66-64 %, respectively, of the national average in the region of Northern Hungary.

<sup>1</sup> EU Commission Communication, (06.10.1996.)

In the regions the rate of employment in agriculture changed between 8% and 21 % in 1999-2003. In the region of Northern Hungary the indicators for the period show a standard deviation between 8% and 10 % with a decreasing character in time.



Source: Regional Statistical Yearbook, 1999-2003.

Figure 3. Employment in agriculture in the regions in Hungary against total employment

### The role of agriculture in the national economy

International experience shows that in parallel with the development of the economy the role of agriculture in the performance of the national economy shows a declining tendency. This decline can be partly counterbalanced by giving priority to quality developments, which is a fundamental requirement of the European Union in every sector of agriculture. The issue of the effectiveness of rural development is connected to this as it is determined by the employment role of agriculture.

The weight of agriculture within the national economy has decreased in Hungary in the past decade as well. The loss of its economic role took place not only as related to the other sectors but also in the absolute values of expenditure and performance as well.

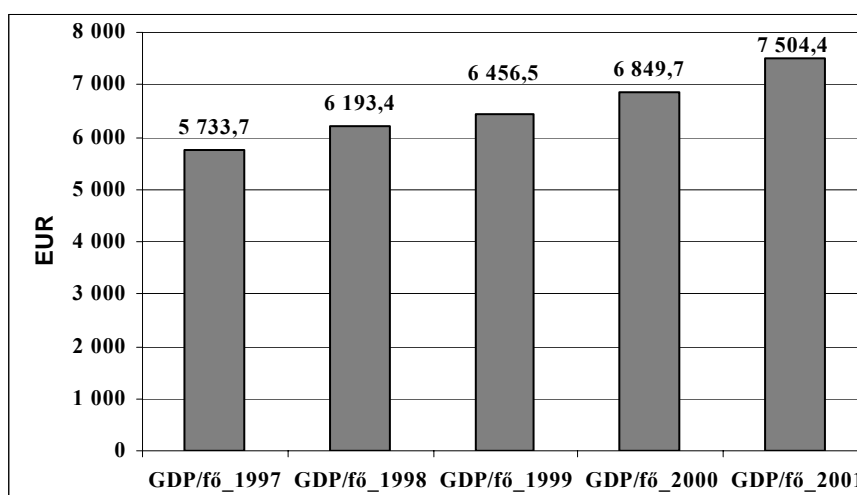
Year	The rate of agriculture				
	in GDP production	in consumption	in exports	in investment	in employment
	At current prices, %				
1990	12,5		23,1	8,7	14,2
1991	7,8		25,1	4,3	11,9
1992	6,5		26,0	2,9	11,3
1993	5,8		23,4	3,1	9,1
1994	6,0	34,0	20,6	2,9	8,7
1995	5,9	34,5	22,0	2,9	8,0
1996	5,8	33,1	18,4	3,4	8,3
1997	5,2	33,3	13,0	3,6	7,9
1998	4,9	33,1	10,5	5,5	7,5
1999	4,2	32,5	8,0	5,2	7,1
2000	3,7	28,6	6,9	5,0	6,5
2001	3,8	29,6	7,5	6,2	6,2
2002	..	..	6,8	..	6,2

Source: Central Statistical Office, Agricultural production 2003.

Table 1. The rate of agriculture in the national economy

### The position of the region of Northern Hungary

The per capita gross national product is two thirds of the national average, and the rate of employment in agriculture is 8-9%.



Source: Regional Statistical Yearbook, 2003.

Figure 4. Development of per capita GDP in the region of Northern Hungary



The prospects for the development of agriculture are good in the region. In the south, in areas belonging to the Great Plain, wheat and corn production is possible, the areas at the feet of the hills are excellent for quality grape production, and the areas on the hills are suitable for high quality fruit production, forestry and game keeping. Despite the favourable potentialities, agricultural production has substantially declined in this region as well, with only grape growing keeping up its previous position. (3)

The agricultural production structure of the regions should be most profitably transformed towards a structure matching the ecological potentialities. As can be seen from Table 2, the activity structure of the agricultural businesses in our region has hardly changed in the three years under examination.

Region	Plant cultivation	Livestock farming	Mixed	Plant cultivation	Livestock farming	Mixed
	Gazdaságok aránya (%)			gazdaságok aránya (%)		
	2000			2003		
<b>Total of the economy</b>						
Central Hungary	40,87	30,36	28,77	38,83	29,84	31,33
Central Transdanubia	48,86	18,94	32,20	49,09	19,18	31,73
Western Transdanubia	48,35	10,66	40,99	51,19	12,57	36,23
Southern Transdanubia	44,50	14,55	40,95	42,01	17,25	40,74
<b>Northern Hungary</b>	<b>44,27</b>	<b>23,45</b>	<b>32,28</b>	<b>45,28</b>	<b>25,72</b>	<b>29,00</b>
Northern Great Plain	35,05	24,27	40,68	31,35	26,96	41,69
Southern Great Plain	30,30	26,31	43,38	24,94	31,15	43,91
<b>Total</b>	<b>39,72</b>	<b>21,93</b>	<b>38,35</b>	<b>37,60</b>	<b>24,43</b>	<b>37,97</b>

Source: Central Statistical Office, Agricultural production 2003.

Table 2. Distribution of agricultural businesses according to types of production and regions

It seems essential to find the activities – for the individual regions – that best meet the aspects of employment, income and sustainability. Magda-Marselek (1999) plans the following types of agriculture for each small region:

- profit-oriented – in areas with better than average potentialities,
- extensive – production sustainable with minor state subsidies,
- social – production maintained for employment purposes.

In the paper Foundations for the Agricultural Aspects of National Country Planning of 1998, after considering the different potentialities of the individual regions, and with the intention of dissolving the existing regional tensions, the authors propose agriculture of different types for the individual regions that is similar to the above classification:

- competitive, profit-oriented agriculture in areas with good potentialities,
- production in specialist production areas that takes advantage of the special potentialities of smaller areas (e.g. vine growing regions),
- extensive agricultural cultivation for the utilisation of marginal areas with moderate potentialities,
- social-type agriculture improving employment in small regions particularly severely hit by unemployment,
- agriculture for family subsistence and improving local supply, which is essentially related to traditional small farms,
- withdrawing agriculture in areas with the weakest potentialities where the current plough-land-based agriculture will be gradually replaced by forestry and grassland agriculture,
- agriculture with protective functions (environmental protection, nature conservation) mainly in areas of nature conservation and environmentally sensitive areas. (4)

#### **Development potentials of the region of Northern Hungary and the agro-economy**

The general loss of scope of the agriculture, the shift of the economic structure towards the tertiary sector, the increasing problems in employment and the resulting social tensions all lead to the need that some alternatives should be found for agricultural areas, for the people living and working there so that they can manage in the future. This, however, is not only a sector problem, for it affects the economic capacity of performance of the region.

Fehér (1996) set up the following groups of economic areas in the region of Northern Hungary according to the location of regional crises and the adjustment of agricultural producers. The indicators used in the study were as follows:

- per capita gross income,
- regional agricultural potentialities,
- rate of persons employed in agriculture,
- rate of rural unemployment.

Groups of areas	Regions in Northern Hungary
Regional crisis area	Bodrogköz; Közép-Tiszavidék – Hevesi-ártér; Északi-Bükk – Ózdi-medence – Tarna-völgye – Tardonai-dombság; Északi-Cserhát – Központi-Cserhát – Zagyva-völgye; Közép-Tiszavidék – Borsodi-ártér; Központi-Mátra; Borsodi-dombság – Hevesi-dombvidék – Cserhát; Felső-Tarnai-dombság – Mátralába; Nyugati-Cserhát; Bódva-völgy;
Potential crisis area	Tokaji-borvidék; Keleti-Cserhát – Hatvani-sík; Hegyközi-dombság – Zempléni-hegység; Gyöngyösi-sík; Nógrádi-medence – Galga-völgy; Abaúj-Hegyalja – Szerencsköz;
Area in average situation, but sensitive to crises	---
Adaptable area with relatively well-developed agriculture	Észak-Alföldi-síkság – Taktaköz; Bükkaljai és Gyöngyösi borvidék; Hernád-völgye; Egri-borvidék;

Source: Fehér (1996)

Table 3. Division of the economic areas in Northern Hungary according to the different economic adaptation of agricultural producers

Development may have the following general tasks in the county of Borsod-Abaúj-Zemplén: (6)

*Agricultural aspects of regional crisis management:*

- Among instruments promoting short-term employment, financing by the central budget of public/communal works in forest planting, countryside maintenance and road works seems to be a solution suitable for solving tensions in employment. Measures of agricultural employment with longer term effects can only be envisaged in conjunction with other crisis management solutions.
- Priority support for farmers with secondary and tertiary professional qualifications in agriculture undertaking definite agricultural activities as a career in the crisis areas in their settlement and in establishing their businesses, and exemption from central taxes (corporation tax, personal income tax) for a definite period. With the stabilisation of their income situation, taxation can be solved by means of the local taxes, which would assist the allocation of local and regional funds as well as bring the capacity of the companies and the local development demands into greater harmony than the current system can.
- Reinstitution of the interest of agricultural producers in income, turning negative gross incomes into positive ones by individual measures, and ensuring a minimum standard that will enable young entrepreneurs and start-up enterprises to cope with their initial problems.
- The launch of special social land projects should be considered in villages where social agriculture providing part-time employment and subsistence is also needed in addition to profit-oriented, competitive agriculture.

*Development and operation of knowledge, skills and technology transfer:*

- Training for farmers, modernisation of the county counselling and information system.
- Elaborating and application of EU-conform farmer accounting systems.
- Developing an agricultural technology centre for Northern Hungary, support for research providing a foundation for rural development and sustainable agriculture, and support for the development of environment-friendly technologies.
- Promoting civil organisations, developing international relations in rural development, organising exchanges of experience.

*The expected role of agriculture in employment:*

- Agriculture in and by itself will not be able to solve tensions in employment in any area of the county whatever the developments in farm structure, production structure and production standards.
- The future changes in employment in agriculture depend primarily on the development of production structure, on the possibilities of vertical production expansion and diversification.
- In smaller villages, due to deficiencies in supply and also to the traditions, agriculture with the primary purpose of family subsistence will continue to exist, which will not improve employment, but take advantage of the fractional labour force and reduce the expenditure of the families on food.
- Non-traditional cultures (e.g. herbs), and breeding new animals (e.g. silk worm and rabbits) as well as special production methods (organic production) can be taken into account as activities expanding employment.
- The target for farmers close to the cities is to reclaim their positions lost in the local markets. The development of the belts providing food for the cities offers a possibility for expanding employment, not to forget about its impact on food prices
- The possibility for diversifying the activities of agricultural plants towards non-agricultural activities is usually limited, but it greatly varies from region to region and even from village to village.

Even in the medium term a reasonable attraction of the areas in the county is to be established both towards the population living there and towards the people arriving there. Developing a freer and more controlled path for the flow of persons, market, services and information is a fundamental condition for that purpose.

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## **A MYSTERIOUS SPELL OF BRANDS**

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The terms brand and brand development are constantly evoked and mentioned in the marketing literature. The essence of marketing is often defined as brand management and thus, brand is believed to be the marketing factor of success.

A lot of emphasis is laid usually on the importance of brands. On the other hand there are undeniable evidences that classical brand-oriented customers tend to ignore brands, which results from the fact that there are not great differences in qualities of products, commercial brands, brand communications and 'action-orientation' processes. This change in customer behaviour can be experienced both on national and international markets. As it is a world phenomenon, several experts ring alarm bells in leading market economies in Western Europe. I think these tendencies endanger only poor and ill-designed brands as well as unsuccessful companies. Whereas the success of well-established and popular brands is greater than ever.

To take advantage of this fact is possible only if building a brand image is considered to be a conscious research activity and appears in the form of marketing investment built on multi-sided analysis of consumer-customer behaviour and efficient, integrated marketing communication activities, the objective of which is to increase the market value having an essential role.

There are myths about brands, their origin and development saying that it is difficult to give an explanation to reasons of their strengths and values as they are results of a 'magical activity'

### **Functions and business roles of brands**

The conventional role of a brand is to identify a product and link it with the manufacturer and supplier as well as to demarcate it from other products, which promotes the positive decision making processes of a buyer. (Bauer-Berács, 1998)

It is commonly known that the role, the usefulness and the importance of brands considerably contribute to the business success and enterprises do not doubt this. There is nothing surprising in the fact that in the past several decades the practice of branding has shifted from classical consumer and FMCG products towards investment goods, namely B2B products, services, cultural events, festivals, civil organisations, towns as well as political organisations.

On stagnating markets and in the cases of price consciousness of customers brands of any product types are especially important factors of success.

A brand is able to produce value surplus for both customers and sellers. Brands provide assistance to customers with information analysis and processing, reduce customers' risks, and decision-making uncertainty. Their main properties are continuity, visualisation and their not interchangeability. Brands are associated with confidence and quality consciousness, both of which contribute to the increase of brand awareness, loyalty and identity

A brand bears a considerable value for both sellers and the manufacturers as

- it is a factor of competitive advantage,
- it sets market boundaries for competitors,
- it enables the seller and the manufacturer to set and increase their prices ignoring competitors,
- it enables them to launch more effective and cheap marketing and selling campaigns,
- it conveys key information to its customers,
- it results in customer loyalty,
- it improves the business position of a company and other products can benefit from its strength,
- it can increase the profitability of a company,
- its value both increases the success of the company's performance and appears in the form of capital.

The marketing theory as well as practice knows a lot about brands and their effects. In the past several decades the conscious brand building has become possible due to results achieved in marketing, especially in consumer behaviour and basis of marketing behavioural science, in which German scientists have achieved considerable results. (Trommsdorf 2000, Kroebel-Riel 1995)

If we want to decide of something whether it is a brand and what brand it is, we have to take into consideration the opinion of targeted customers and consumers, that is we have to find out whether they experience the unique features of the product, its distinctive marks and can define the special composition of its advantages. Only after this the opinion of certain analysts and suppliers can be evaluated. In the case of successful brands it is the quality, innovation, emotional surplus and uniqueness that counts.

Success stories about brands are related to major, global and well-established brands. We can often read about weaknesses of Hungarian brands, their disappearance from the market, their weaknesses and survival due to privatisation. (Berger 2003). However, it is worth mentioning that owners of successful, ambitious and new brands do not always make sufficient efforts to make the national and international public know that there is a Hungarian product. This can be explained by Hungarian consumer behaviour, low level of consumer ethnocentrism, attitudes to brands and unsatisfactory and poor marketing activities of most Hungarian companies as well as their neglecting the factor of consumer confidence.



At the same time it is essential for entrepreneurs to be aware of the importance of brand values, which is not only the basis of their business success, but the most efficient tool to be used for the increase of their company's assets and share value.

This awareness plays a crucial role in laying the basis for strategy and tactics development and using the best decision alternatives needed by entrepreneurs when they have to make sound decisions regarding investments into brands and compare these investments with the other ones. A brand should not be only a hobby of marketers, but it should be a serious company tool used by managers in decision-making and action.

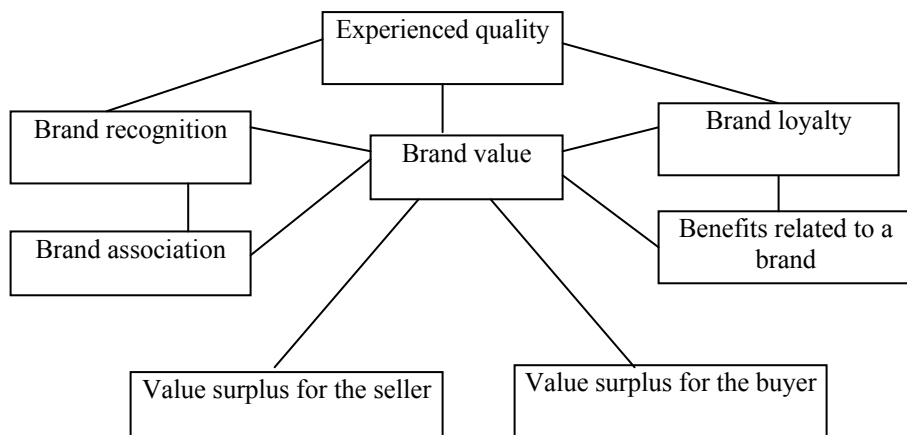
**The unity of twofold interpretation of brand value**

Brand value is a complex category, which on the one hand has a monetary value, a psychological customer value, and a popularity value, an image value and a confidence value on the other.

Brand as capital also emerges in the heads with the help of emotions. When we talk about benefits of brands experienced in every day business processes, brand values and their consequences , we can find the basis for defining the capital value.

The classical constituents of a brand value (Aaker 1996):

- brand recognition,
- brand association
- experienced quality,
- benefits related to a brand
- brand loyalty



Brand recognition is the extent to which a brand is known and loved by consumers (spontaneous recall, aided awareness, actual top-of-mind) Brand recognition is the basis of brand associations. The essence of a brand association is as follows:

- emotions and thoughts related to a consumer and brand,
- community of a customer and a brand where
- consumers look for brands which are a close match with their own personality and have
- such brand identities as core values that customers are attracted to

Brand association is the basis of brand extension, which actually means imposing a brand name on new products or group of products in the following ways:

- horizontally within a product group (packaging, additives)
- vertically within a product group (price, up and down movements of the value)
- cover-branding in the case of new product groups (Old Spice, Pierre Cardin) or common branding in certain cases.

Brand loyalty makes it easier for customers to make their choice and decreases purchasing risks. It ensures secure revenues for companies, a less expensive, but more effective marketing and provides considerable assistance with attracting new potential customers.

### **Monitoring trends and judgments in brand building**

Market values are created in heads on the basis of emotional experiences and information fed about pictures, music, life and experience without 'overloading' consumers with text messages. (Trommsdorf 2002)

With the help of marketing communication they can be implemented, integrated and put in line with consumer trends, technologies, social effects and their understanding.

Trends playing an important role in brand building are as follows:

- changes and transformations in demographic target groups, especially in age and family structures,
- further polarization of consumer demands,
- intensive market segmentation resulting in disappearance of conventional market segments and their customers. There is a paradox in behaviour as depending on the demand and supply customers purchase both premium and poor brands.
- Products suffering from low demand experience decrease in brand loyalty. More and more people think that 'all brands are similar'. (e.g. 50% of the young in France have the feeling of success when they wear their favourite brand. This figure is only 20% in Germany). (Trommsdorf 2002)
- Further convertibility of brands supported by standardisation of quality.
- Most brands (85%) belong to the active category positioned in the middle and experience steady and wide demand.

- There is a merger of brands resulting in disappearance of some (decrease in the brand number of Unilever) and in highlighting the demand for rational brand management.

It is almost impossible to create a brand on the basis of quality, as quality is becoming a standard and is not suitable for being the final reason for doing the shopping. Brands need experience-dimensions in order to be able to demarcate themselves from competitors both physically and functionally.

Thus, brands are investments assisted by communication. Integrated market communication is an important means used for promotion of brand values. The unity represented by IMC is used for creation of credible and sustainable brand image. It is very essential to mention that integrated marketing communication should not be considered to be buyer-oriented and or something that deals only with integration of tools. Integrated marketing communication must primarily be recipient and customer oriented and find out what and how emerges in customers' heads . Only after doing this we can speak about integration and harmonisation of marketing tools.

All these interrelated concepts highlight the need for laying the foundation for brand building and marketing research (receptivity examinations, conjoint analyses, attitude researches, life style analyses, trend researches, etc.) on the basis of which conscious communication strategy, complex and accurate brand policy solutions can be conducted.

### **Measuring brand values**

It seems reasonable to ask whether the brand value is an unknown factor or can be measured. The realistic value of the brand would be crucial to know, as values of certain brands often exceed values of the infrastructure assets of the whole company.

Brands often change masters as a result of privatisation not only in Hungary (chocolate brands like Szerencsi Boci, Sport szelet, etc.), but on international market as well (e.g. Adidas, Puma, Seat, Jacobs). Financial experts are in dilemma when they have to prepare materials for contracts (Philip Morris paid 90% for brand when it bought Kraft. The brand value amounted to \$12,9 billion).

Brand values are not measured when sales agreements are prepared, but provide basis for continuous business evaluation of a company and its performance on the stock exchange

Evaluations made by various agencies may show different results. Nowadays evaluations are not reliable, e.g. in the case of Coca-Cola the figures ranged from \$33billion to \$83 billion (interbrand rates). Divergences in financial data provided by different evaluation methods and mechanisms may lead to serious consequences resulting in bewilderment of entrepreneurs. A German journal states that there are 30 consulting firms on the market in Germany, but it is difficult to judge whose

evaluation is reliable. According to a research 64% of German companies have already had at least one evaluation made, 19% have evaluations made on yearly basis spending huge sums of money on it, generally 50 000 Euros. The evidence of uncertainty in evaluation is proved by the 70-20-2-type conclusion, meaning that 70% consider brand evaluation important, almost 20% know the best processes and only 2% use them. (Schimansky 2003)

As it has already been mentioned in the discussion of consumer trends and habits lot of 'brand processes' are unknown or not well explored.

Brand evaluation which has to be built on consumer and customer opinions as well as their behaviour evaluation is a difficult task as, for example, only in Germany there are 500 thousand registered brand names, out of which only 50 thousand are active and every day about 300 brand names compete for as favourable position in the buyers' heads as possible.

Processing and evaluation of 'information and emotions' not mentioning the brand names used in competition is a serious trial, as generally people use about a thousand words.

I do not agree with those who apply the evaluation mechanism used in estate industry for monetary evaluation of brands. The subject matter of evaluation in the case of real estates is obvious, but brand is difficult to define and understand.

There are scientists who lay emphasis on the importance of legal protection and in the end come to quite different conclusions.

In order to be good at methods to evaluate brands and to have a objective attitude to your own brand or brands you should set criteria and define features which determine a really good and realistic value:

1. The value of a brand lies in its usefulness, how it is used, utilized, how much its return and surplus is produced.
2. The value of a brand lies in its future. Both the current and the potential data are basis for calculations.
3. Brands mean competitive advantage, have an impact on customers, lead to increase in demand and as we have seen they have other strengths as well. Tangible and intangible assets also play an important role in this. Not all the surplus yield comes from brand values. They have to be distinguished and split and figures have to be corrected.
4. The price of a product does not depend only on the brand, but on the performance. A brand name can reflect a cheap product (Aldi, Dell).
5. Brand investments do not become brand values at once. if we want to determine the brand value from the costs spent on brand building, we won't get any reliable indicators.

6. Brands ensure potential income and are often identified as a single constance linking element existing between a company and a buyer. Brands represent performance, previous experience, create customer loyalty and ensure future demands. The future of poor and risky brands considerably differs from the well-designed and established customer-related brands.
7. Brands do not serve homogeneous markets. Customer-brand relationships are different in submarkets (geographical location, product, selling specialities, evaluations ignoring market segments are not accurate, do not give insight into evaluations of certain markets and market segments.
8. Brands fulfill their functions without time limits if they are properly invested into. Thus, evaluations taking into account time limits underestimate them.
9. A brand is more than just a trademark. Its essence lies in ensuring customer relation and demand evaluations laying emphasis on lecal protection are not correct as licence fees do not constitute the basis of evaluation.
10. Brands are always unique and do not depend on relations or situations. They are really special in the way they and other equity elements perform their functions and exert their influence. For example, Apple and Dell brands have completely different identities. Methods which compare them to other brands are not reliable or acceptable.
11. Brands are complex and their evaluation cannot be done mechanically or built on standard and general elements. There should be a special approach.
12. Brand evaluation is a professional and scientific task built on business experience, information, research and marketing methods. This is art. It is not enough to compare the assets in the balance sheet with the stock market prices and in this way receive brand values of a company as Trommsdorf says. (Trommsdorf 2002.)

Market-oriented evaluation is built on customers and wants to explain why the brand is strong and how to increase its value. The McKinsey- Markenmathik model (elaborated in cooperation with Marketing Center at Münster University) meets the criteria mentioned above. It evaluates strong and weak points of a brand image, the turn-over potential of a brand, identifies brand properties and offers precise actions. The method begins with segmentation and evaluates the brand image according to these segments.

It can be stated that brand is often the most valuable asset element the extent of which is huge and requires investment in the future.

### **The need for brand building in order to contribute to the success of small and middle-scales enterprises**

The theory and practice of marketing owes small and middle scale enterprises with professional brand policy. The fierce competition and the assession to the EU have created more open markets with new members. As for the companies creating uniqueness and orientation is a must so that they cannot be confused. Only few companies have grasped this opportunity This can be achieved by investing lower

costs in marketing and communication than expected. Activities of small and middle scale enterprises have to be promoted as their competitive advantage can be achieved only by developing sustainable brands, business relationships and not by individual customers.

Customer satisfaction, establishment of reliability and brand building can be successfully implemented in companies and enterprises which have realized that investing into marketing and brand is as important as investment into machines and other assets. The development of marketing methodology contributes to professional, scientific market policy of KKV utilizing the results achieved in marketing research.

Brand management raises several problems and difficulties as:

- New brands often experience failure (food industry 85%)
- There is a huge number of manufacturer brands that extinct as consumers look for their own identity in differentiation of supplies and shopping.
- Tradors will become more important than producers (shop loyalty, supply differentiation, exclusivity).
- Brands without surplus will disappear, thus there is a need for building differentiated brands.
- Death of brands starts from insight, with weaknesses of an enterprise:
  - with brands without functions, when there is no real 'brand core',
  - with brands without identity.
  - with brands without creativity,
  - with brands without colleagues or workers,
  - with brands without sustainability (fractal)
  - with brands without management and investments

Taking into consideration all the factors mentioned above it can be concluded that the mysterious spell of an established brand remains , not because of something magic, but due to conscious and carefully planned marketing work.

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## **A Short History of the Publications of the University of Miskolc**

In 1929 the legal predecessor of the University of Miskolc in Sopron started the series of university publications with the title *Publications of the Mining and Metallurgical Division of the Hungarian Academy of Mining and Forestry Engineering* (Volumes I.-VI). From 1934 to 1947 the Institution had the name Faculty of Mining, Metallurgical and Forestry Engineering of the József Nádor University of Technology and Economical Sciences at Sopron. Accordingly the publications were given the title *Publications of the Mining and Metallurgical Engineering Division* (Volumes VII.-XVI.). For the last volume before 1950. - due to a further change in the name of the Institution - *Technical University, Faculties of Mining, Metallurgical and Forestry Engineering, Publications of the Mining and Metallurgical Divisions* was the title.

For some years after 1950 the Publications were temporarily suspended.

After the foundation of the Mechanical Engineering Faculty in Miskolc in 1949 and the movement of the Sopron Mining and Metallurgical Faculties to Miskolc the Publications restarted with the general title *Publications of the Technical University of Heavy Industry* in 1955. Four new series - Series A (Mining), Series B (Metallurgy), Series C (Machinery) and Series D (Natural Sciences) - were founded in 1976. These came out both in foreign languages (English, German and Russian) and in Hungarian.

In 1990, right after the foundation of some new faculties, the university was renamed to University of Miskolc. At the same time the structure of the Publications was reorganized so that it could follow the faculty structure. Accordingly three new series were established: Series E (Legal Sciences) Series F (Economical Sciences) Series G (Humanities and Social Sciences). The latest series, i.e., the series H (European Integration Studies) was founded in 2002.

Business Studies Volume 3, Number 1 (2005) well represents the different aspects of the research activity of the Faculty of Economics, University of Miskolc. We believe that the philosophy of the Editorial Board and the competence of the authors shall guarantee the high professional level and the up-to-dateness of the publications. We also hope that this periodical will contribute to the international reputation of the University of Miskolc.



## **Business Studies**

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