

# **ROMANIAN ECONOMIC AND BUSINESS REVIEW**

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**THE EU POSITION IN THE WORLD ECONOMY IN THE CONTEXT  
OF CURRENT ECONOMIC CRISIS: REFLECTIONS ON THE  
G20 MEETING OF APRIL 2009**

Florin Bonciu\*

**Abstract**

*The article focuses on the changes in the economic balance of power in the world economy, particularly as result of long term trends related to globalization and in correlation with the implications of the current economic crisis. The analysis is done in the framework of the G20 meeting which is attempting to design a new system of international institutions, compared with a new Bretton Woods. The paper concludes that the position of European Union in the world economy is gradually declining and that steps are to be taken in order to change this trend.*

**Keywords:** European Union, G20, economic crisis, Bretton Woods II, world government.

**JEL Classification:** F15, F59, O17

Starting mid 2008 the world economy has been confronted with a crisis that has been unanimously labeled as “once in a century” (1). Because globalization means universal interactions, both in positive and negative aspects, it is unavoidable that the crisis affects all countries and, as result, requires world wide actions (2).

It is in this context that an interesting phenomenon can be noted, the fact that Europe as an entity represented first and foremost by the European Union is somehow a secondary actor (3). This observation can be demonstrated by the increasing relevance of G20 as a debate forum on world economic issues (4). G20 which has been established a decade ago, in 1999, was until last year a rather obscure organization, at least for the public opinion. Nowadays it is mentioned with increasing frequency as the relevant organization that brings together the countries able to find a solution to the crisis. As the name shows, G20 consist of 20 entities, which are: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the United Kingdom, the US and the EU. Out of the 20 entities, only 6 represent Europe (France, Germany, Italy, United Kingdom and

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the EU), while 14 represent other parts of the world. What is even more relevant is the fact that in various business or political circles there are people that speak about G2, that meaning United States and China.

This comment may seem just a speculation but it is backed by economic data. The share of Europe in world GDP declined from 19.5 in 1994 to 16 % in 2008.

This is the result of many years before the onset of the crisis when European economy grew much less than the economy of United States or than countries from the Pacific rim. European companies are bought by investors from India, China, Russian Federation or countries from Middle East and support for the difficult situation of banks are sought in China or other parts of the world. Examples can continue, and as economic crisis is the main subject, it is to be noted that while USA and China have taken massive fiscal stimulus packages which reached 12 % of GDP in the case of USA, in Europe the corresponding measures represent a mere 1.5 % of GDP (5).

It is in this context of the long term decline of the European role in the world economy that the G20 meeting takes place in London on April 2, 2009. The key objective of this summit is to restore global economic growth through enhanced international coordination. Based on previous discussions and analyses three commitments are required from the part of all participants:

- Implementation of all actions which are necessary to stabilize financial markets and thus to help economic actors get through the recession;
- Reform of the global financial and economic system in order to restore confidence and allow re-launch of economic activity;
- Generate sustainable growth, high levels of employment and poverty reduction in the global economy.

It is also interesting to note that the global scope of crisis and its depth has determined a reaction at the level of international organizations like United Nations. It is in this context that a greater role and greater funds have been assigned to the International Monetary Fund and that the Millennium Development Goals of the United Nations are somehow included in the objectives of the plan to rescue the global economy. One can say that global problems raised the importance of global institutions and this again means less role for the European Union.

As result, at the G20 summit, the main topics on the agenda may refer to (6):

1. The need of a fast completion of the current global trade negotiations, the Doha Round, in order to strengthen the commitment to refrain from protectionist measures;
2. The solutions to ensure that everyone has the skills they need for the jobs of the future;
3. The need to correlate economic recovery to a shift towards a low carbon economy;

4. The establishment of a strategic framework to stimulate investment;

5. Commitment to the Millennium Development Goals and therefore increase of development assistance. On this last topic it is to be mentioned the position of George Soros who said that the G20 meeting had to come up with concrete solutions to help the developing world in particular, which had been worst hit.

One reason why the G20 summit in April 2009 is relevant for the European Union is the fact that discussions refer to the reconstruction of the world financial system from its foundations up. Maybe the G20 Summit in April 2009 would not be exactly a Bretton Woods II but that would be the essence of the discussions. And at these discussions European Union would be far from a key player if any at all.

Just before the summit the UK Prime Minister called on world leaders to 'seize this time of profound change to forge for our generation a new internationalism, a new era of international cooperation that is both hard-headed and progressive.' (7).

Today 70 % of world economic growth comes not from the older industrialized nations but from the emerging and developing countries, and that is why there must be a new deal that includes every country and every continent.

As result of this new situation in the world the longer-term reforms of the international financial architecture may imply that, as Mr. Gordon Brown, the UK Prime Minister, said: 'The next head of the World Bank need not be an American. The next head of the International Monetary Fund need not be a European. We must make the governance systems of the World Bank and the International Monetary Fund more transparent, more relevant and more open.'

A similar view has been expressed by the UN Secretary General, Mr. Ban Ki Moon, who considers that the Bretton Woods institutions must reflect the current economic and political landscape: 'If we are asking rising economies such as India and China to support our global financial institutions, we must give them a broader voice in their management.'(8) The implications of this fact is that the position of participants in the world financial institutions which are giving less support (i.e. European Union) will decline.

Before the G20 summit consultations took place with leaders of countries not participating directly to the summit from Asia, Africa and Latin America. As a common denominator these leaders had two concerns: the maintaining of a global free trade system and the avoidance of a situation in which the G20 summit would generate a solution only for the participants.

Summing up these concerns one can say that in a global economy, faced with a global crisis, there is a need for a global system able to provide a global solution. That means, in other words the raising up of integration to a new, global, level. Such a level may be a sort of one world government in the making which

may render obsolete the idea of continental integration. If such a case would be, then that can be a lesson that history does not move in uniform way, with an uniform speed, but rather jumps from one level to another.

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**SELF SERVICE TECHNOLOGIES SPEAK FOR THEMSELVES**

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Iulia Furdui\**

**Abstract**

*The paper analysis the main criteria for successful self service technologies.*

*Self service technologies are changing the way customers interact with companies. As a result, a lot of firms are developing innovative self service technologies with hope that their customers are satisfied. In order for a self service technology to succeed in making customers happy, companies must learn and know what drives customer satisfaction.*

*This paper examines what a firm should consider in order to encourage customers to at least try, and eventually adopt, the self service technology offered by a firm into the customer's regular routine. Factors that encourage the customer to try a new self-service technology for the first time and factors impact customer satisfaction and dissatisfaction will be addressed.*

**Keywords:** *self service technologies, customer value, customer satisfaction*

**JEL Classification:** L80, M20, M31,

**1. Introduction**

Nowadays, a trip to the bank, supermarket, or airport shows a growing presence of self-service technology. Although these systems will never replace personalized customer service, they are extremely flexible and offer an increasing number of consumers fast and reliable service. High-end and trendy hotels have begun to see a role for self-service in their businesses. A growing number of chain hotels are using the technology as a way to maintain service excellence during peaks in guest traffic.

Constantly, retailers are increasingly trying to innovate options for delivering service to their customers and to make it easier to use and more helpful.

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The infusion of technology is dramatically changing the nature of service which has been traditionally used by retailers. By providing a self service solution that is easy to navigate and quick to produce the most accurate answers, high technology companies ensure costly telephone contact with the call center is reduced and customers quickly find the answers they seek.

Companies try to convince the customers that the use of technology is simple, faster and easier. They achieve this by advertisement and creating awareness as well as demonstration of these technologies.

## **2. The challenges of 2009**

The slowdown in economic activity in developed countries was the major factor in the reduced expansion of global trade in 2007. This trends combined with effects of the financial markets during last year detonated the global economic crisis. The variation in real trade growth among regions remained large, reflecting marked differences in economic activity and relative price developments.

This crisis will have an effect on both merchandise markets and services markets. Last year the global GDP growth was forecast between 2.5 and 3 per cent. This pessimistic outlook was more optimistic then everyone believed. This economic crisis is based primarily on adverse developments in the financial markets, the dramatic downturn in the US property market, the decline in inter-bank lending and the dwindling capitalization of major stock markets<sup>1</sup>.

This year money, few like they are, will move away from bricks and mortar stores. Investments will be focused to the online experience. So we'll live in an online virtual world because the real world will be full on frustrating events. And this trend to the web and e-services is just as true in non-profit sectors as it is in retail. In downturns, more people head to higher education, as governments continue their move to e-government practices and everyone looks for ways to reduce costs. Getting the customer to serve themselves rather than involving costly manual processes should be a no brainer. Nevertheless, many business cases in 2009 will focus on self-service - often as a knee jerk reaction, sometimes as part of a longer-term, planned strategy.

People who have more highly qualified jobs and education levels, tend to display a more quantitative time orientation as reflected in the time statement "time is money", which will lead them to attach more importance to the time gain that comes with using self-service technologies.

Shifting data management to the customer also lowers a company's overhead costs by reducing the number of customer service agents needed and allowing

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<sup>1</sup> International Trade Statistics 2008, World Trade Organization Report

existing personnel to focus on higher volume activities, such as targeted marketing<sup>2</sup>.

## **2.1 Self service era**

Self-service is a version of electronic support that allows customers to access information and perform routine tasks over the Internet. More and more frequently, businesses are implementing self-service applications to improve their customer service and reduce costs. Browse these buzzwords and brush up on key self-service definitions and terms.

Self-service technologies refer to services that are performed by customers themselves using various types of technological innovations, such as ATMs, the Internet, touch screens, and interactive kiosks. They represent an alternative way of service delivery using innovative technologies for complementing or even replacing personal services<sup>3</sup>.

We have entered the decade of self service. Customers value the convenience, consistency and self control of automated transactions over a friendly smile. Companies value the increased coverage, low cost of operation and reliability of automating transactions.

It is common practice for individuals to encounter inexperienced sales people, long lines and companies that are closed when you want to do business. As a result, opportunities to conduct transactions online or using self service technologies have become a welcome alternative to most consumers.

### **2.1.1 Evaluating self service technologies**

In order to succeed on the self service technology market, the companies should focus on customer satisfaction, by answering the following questions:

- What do consumers want most from any service experience?
- What percentage of consumers prefer self-service over full-service?
- How much do age and gender affect consumer attitudes toward self-service?
- Do tech savvy consumers really use self-service devices more often?
- What factors lead consumers to choose self-service over full-service?
- What factors lead consumers to choose full-service over self-service?
- What self-service devices do consumers use most and which do they use least?
- Are consumers satisfied with their self-service experiences?

When evaluating self service technologies, companies need to consider all costs related to implementation, not simply development and deployment. Count

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<sup>2</sup>Self-service technologies help companies help themselves, by Cindy Atoji, 04.25.2007

<sup>3</sup> Self service technology: top five buzzwords, Amanda Malgeri, nov.2007

on a long term commitment to maintenance and create feedback system that tracks the self service products customers use to resolve their issues.

Companies need to educate continuously the customers about the benefits of using the self service technologies. They also need to provide support and answer all the questions concerned the usage of innovative technologies.

## **2.2 Advantages and disadvantages of self service technologies for customers**

The main advantage of using self service technologies is to be able to conduct a business 24hours/7 days and easy access to global marketplace.

The ability to access and control information raises customer satisfaction, whether it's conducting a banking transaction, checking cellular minutes, ordering an on-demand movie or requesting time off. Self-service empowers people to do things on their own.

It is true that the self service technologies reduce costs, but, in the same time a weak point is that you cannot build such a strong relationship with the customers. In the past, most of the companies had strong relations with the customers but nowadays, because of the new technologies these relations are hardly happening. It is cheaper to keep an existing customer than to win a new one. Satisfied customers are customers that are more loyal and it is easier than ever to spread the word about a poor customer experience.

## **2.3. Advantages and disadvantages of self service technologies for companies**

Reducing costs and improving services are two primary reasons organizations are putting in self-service applications. Self-service solutions are freeing HR staff from low-value activities, thus allowing them more time to focus on high value, strategic activities that foster improvements in human capital management, especially strategic services around staff development and other talent management services<sup>4</sup>.

Self service technologies continue to expand and improve and costs have come down for many. In fact, self service technologies typically show a return on investment within the first year of implementation.

As terms like “full service” and “self service” become synonymous, related technologies wireless internet become commonplace; and tech-savvy consumers increase their demands for convenience the opportunities and growth for self service technology seems limitless.

Employees think that self service technology is vital to advancement of information gathering in a company and it is very efficient in cutting time barriers and helps them to do more things that make an effort to make money.

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<sup>4</sup> Profitability of self-service technology options: Efficiency gains through the implementation of self-service technologies, Thomas Schröder & [Thomas Rudolph](#), 2007

In the same time, employees feel comfortable and find work easier as it used in the past.

In the same time, the amount of technology used nowadays minimize the number of jobs and gets lots of people fired or just without a job, as in the past people used to do everything the technology is doing now for them.

For employees self service technologies could include<sup>5</sup>:

- time card reporting,
- being able to check benefit status,
- enrolling in benefits,
- change payroll deduction,
- manage career path plans,
- enroll in training classes.

Managers can use this technology in the following directions:

- to approve timecards,
- open job requisitions,
- enter employee reviews online

### **3. Choosing self service technologies**

Self service works when there are benefits for both users *and* the business.

Firms are typically seeking to fulfill at least one of three primary business goals when they choose to enter the self service arena.<sup>6</sup>

**1) Customer service (technology delivered customer service)** -The intent here is to provide the customer service without tying up the company's human resources. If done correctly, it can also save firm money. A few examples of this are: to provide product information to consumers, Internet based package tracking, on-line troubleshooting systems, and phone and Internet banking.

**2) Enabling direct transactions** - customers order, buy, and exchange resources with the firm without any direct interaction with the firm's employees. These sorts of self service technologies include: on-line shopping, automated kiosks, on-line stocks/ security trading, and on-line travel/ticket services.

**3) Educational** - enable customers to educate and train themselves. These include: phone based information lines, information web sites, training videos/DVD/CD and satellite TV-based training

The benefits can be clear; yet challenges remain like where to push information and systems to users without getting pushback, and how to make sense of an ever-changing marketplace.

Firms go in this direction because using self service technologies they are cutting costs and in the same time improving production and service quality.

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<sup>5</sup> Self Service Technology allows HR More Time for Strategic Initiatives, Cedar Group, 2002

<sup>6</sup> Implementing Self-Service Technology To Gain Competitive Advantages, Chang-tseh Hsieh, 2005

Companies that move to self service deliver immediate cost savings in the 18-20 percent range. After the initial investment, most clients see a return on their investment in two years or less. This is a result of improved accuracy in data collection, reduction in time to complete tasks, fewer calls to the HR department and faster turnaround.

While technological hurdles must be passed when implementing new self service technologies, the biggest challenges companies face are often the customer behavior issues. Customer behaviors are ingrained and typically hard to change. The difficulty is that not only must your customers want to change, but also want to take on the responsibility for their own service delivery and satisfaction.<sup>7</sup>

In order to persuade the customers to try self service technologies the companies would create a convenient and supportive environment, with lots of hand holding in the form of first time user help, instructions, FAQ's and online live help. They would be explained the value they can expect to receive by using the self service technologies.

The relationship between the customers and the company is not unlike that between the employees and the company. In the case of self service technologies in particular, customers are co-producers of value, since they are responsible for the service delivery themselves. Taking a fresh look at the customers, and managing them the way you would manage the employees, helps make them better customers by increasing their “readiness” to produce services for themselves.

A research in the field of “who” is using the self service technologies has drawn the following suggestions:

- a positive attitude towards self service technologies determines the customer perception over the easy use, usefulness and reliability of it;
- higher educated customers have a positive attitude towards self service technologies, compared to lower educated customers;
- the perceived newness and the actual usage of self service technologies influences in a higher percentage young people;
- both women and men use the self service technologies, but the perceived usefulness influences more strongly men’s attitude than women’s.

#### **4. Conclusion**

Certainly, the expectations of customer service have evolved. It is thought that life is better, but everyone expects more. Service in other industries, such as airlines, banks and utilities, affects what people expect from customer technology.

There has been a slow realization of the importance of customer satisfaction. However, consumer technology companies are beginning to shift away from their

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<sup>7</sup> Choosing Self-Service Technologies: Ready? Set. Go!, W.P.Carey School of Business , 2007

product-centric focus. Given the low level of customer satisfaction, those that invest wisely could see a big return.

Many companies do not realize the importance of improving the technologies provided to the customers by adding new functionalities and offering more benefits.

The development of self service technology is growing rapidly and the companies are reducing cost and improving productivity and service quality as well as better organization workflow inside the company. Thanks to new technologies the work performed by employees become not only easier but faster and more efficient.

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**CURRENT NEOLIBERAL IDEAS ABOUT EMPLOYMENT AND UNEMPLOYMENT**

Daniela Zirra\*

**Abstract**

*Nowadays there is a wide range of ideas of neoliberal origin about two of the most momentous issues with which are faced contemporary economies, irrespective of their development level. Several scholars point on the ways of measuring and forecasting unemployment evolution or analysis of the relationship between existing conditions of employment and job satisfaction, and other authors attempt to highlight the influence exerted by labour force mobility increases on the occupational-professional sphere. Due to the particular diversity of experts' concerns in the field, our paper focuses on revealing the more significant viewpoints.*

**Keywords:** neoliberalism, unemployment, occupational shifts, job satisfaction

**JEL Classification:** B10, E24, J60

**Introduction**

Nowadays there is a wide range of ideas of neoliberal origin about two of the most momentous issues with which are faced contemporary economies, irrespective of their development level. P. Heyne introduces the unemployment and employment analysis in the context a liberal economic thinking and J. Gershuny approaches the same question for a post-industrial society. Y. Barou and J. Rigaudiat insist on the ways of measuring and forecasting unemployment evolution. C.T.Whelan makes an analysis of the relationship between existing conditions of employment and job satisfaction, and other authors attempt to highlight the influence exerted by labour force mobility increases on the occupational-professional sphere. Due to the particular diversity of experts' concerns in the field a brief presentation of some more significant viewpoints imposes itself.

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## **Analysis of employment and unemployment according to the thinking of Paul Heyne**

Paul Heyne approaches the issues of labour market starting with the negative effects of inflation on the economic life. He considers that one of the most important costs generated by inflation is reflected by and regards the loss of confidence and welfare.

During the periods of economic recession, growth rates are diminished in all economic fields. On the USA territory, by general consensus, the National Bureau of Economic Research has the privilege of deciding, officially the moment in which the slowing down of economic growth changes into recession. Paul Heyne speculates<sup>8</sup>, and justly so, whether all substantial growth slowdowns shift into recession and if perpetual growth is the only way in which economic activity might be developed. Thereby he supports the idea that, by and large, ***the cost of recession is represented by unmet expectations***. The issue is that these are not revealed by the development of aggregated growth indicators, such as the gross domestic product, for instance.

As result of the diminishment of cashed incomes from goods sales during recession periods, the economic agents cut back on output growth rates and downsize the number of employees, inevitably generating unemployment. Hence, recession is a reason of unemployment increase only it does not start from nil nor it returns to nil when the recession period is over. Already in 1944 part of the labour force (1.2 %) was regarded as unemployed in a period when the sixth part of available labour resources were in the army and individuals left school or returned on the labour market from retirement/pension in order to work for six or even seven days per week.

Unemployment does not represent a negative state as long as its level does not exceed natural or frictional unemployment. Therefore, a distinction should be operated between unemployed and temporary jobless individuals, respectively between persons intending to find a job and those who are not satisfied with their jobs and quit them. Assuming that unemployment results from the decisions of economic agents and individuals it should not be presumed that all of them make the right decisions, or that unemployed are content with the situation they are in. In order for the decision taken to be optimal, the individual expectations should be taken into account.

***“The economic Way of Thinking”*** of Heyne is meant to explain the shifts occurred in the evolution of social phenomena, including here unemployment, as consequence of a perception change on costs and benefits of made choices. As result, the Bureau of Labour Statistics makes a clear differentiation between the

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<sup>8</sup> Paul Heyne, *The Economic Way of Thinking*, Eight Edition, Prentice Hall, New Jersey, 1997, in Romanian *Modul economic de gândire*, Ed. Didactică și Pedagogică, București, 1991, pg. 400 - 402

decision of actively seeking a job and the decision to reject the provided opportunity. The general state of the US labour market in the period 1950-1995 as shown by statistical records is presented in **Table 1**. The analysis realised on a representative sample of 60,000 households and by taking into account the entire non-institutional population of 16 years of age and over. The non-institutional population consists of working age economically active and inactive persons (into this category are included unemployed and persons accepting a job, respectively employed). The criteria taken into consideration for a person to be regarded as unemployed are as follows:

- to be in the category of non-institutional population;
- to have been unemployed for the last week;
- to have actively been making efforts for finding a job (in this category are included also persons who shall be recalled to their old job after 6 months, or who shall start working within the next 30 days);
- to be immediately available for starting to work.

Based on collected data the unemployment rate and the employment rate for the considered period of time were computed, and the evolution of these data indicates that unemployment was on increase indicating the incapacity of the economic system to create new jobs.

**Table 1. General Situation of US Labour Market for the Period 1950 – 1995**

Year	Non-institutional population [thou. persons]	Labour force [thou. persons]	Share of non-institutional population [%]	Employed [thou. persons]	Unemployed [thou. person]	Unemployment rate [%]	Employment rate [%]
1950	104,995	62,208	59.2	58,918	3,288	5.3	56.1
1955	109,683	65,023	59.3	62,170	2,852	4.4	56.7
1960	117,245	69,628	59.4	65,778	3,852	5.5	56.1
1965	126,513	74,455	58.9	71,088	3,366	4.5	56.2
1970	137,085	82,771	60.4	78,678	4,093	4.9	57.4
1975	153,153	93,775	61.2	84,846	7,929	8.5	56.1
1980	167,745	106,940	63.8	99,303	7,637	7.1	59.2
1985	178,206	115,461	64.8	107,150	8,312	7.2	60.1
1990	188,049	124,787	66.4	117,914	6,874	5.5	62.7
1995	198,584	132,304	66.6	124,900	7,404	5.6	62.9

Source: Paul Heyne, *The Economic Way of Thinking*, Eight Edition, Prentice Hall, New Jersey, 1997.

The mosaic of unemployment, presented as above, shows however some lacks. First off, it cannot explain why so many persons fail to find the jobs they desire, or why the number of unemployed has increased by 100% in 1995 against 1950, even if in accordance with the presented data the rate of employment increased from 56.1% in 1950 to 62.9% in 1995.

The cost of employment and the costs of taking up a new job<sup>9</sup> differ from one individual to another, depending on certain factors such as: experience, skills, age, family responsibilities, other income sources and possibly the system of values and attitude towards work of each individual. For employers the situation is just as difficult. Adolescents in their training period shall not find acceptable jobs either because they are during their time of studies and have only short periods of time available, or are during holidays, or because the employers consider that the costs for their training would be too high.

The analysis realised by Heyne is rather poor with respect to the field of employment and unemployment, because it is limited to simply juxtaposing these two phenomena, with rather superficial mentions to reasons and factors triggering them. He only makes remarks that one of the reasons for the increasing unemployment rate after 1960 is represented undoubtedly by the decision of the public authorities to provide for social insurance, such as the ones of the unemployment insurance type to an ever increasing number of persons.

### **Occupational shifts in the post-industrial population**

**Jonathan Gershuny** notices the changes in the occupational field which occurred as society evolved from the pre-industrial development stage and the industrial one, where *the services' economy* was operational to the post-industrial state where the way of developing economic activities is called the *self-service economy* (or the economy which develops as result of own and free efforts of the economic agents)<sup>10</sup>.

Gershuny promotes two classification criteria of the occupational field which apparently are identical, as follows:

□ ***Industrial classification of occupations***, after the type of goods and services consumed by the society: manual, technical, clerical, administrative, medical, legal, financial-accounting, etc.

□ ***Occupational classification***, according to the nature of the work, or the share of some occupational categories within the range of occupations at a given time: lawyers, physicians, engineers, accountants, priests, etc.

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<sup>9</sup> Ibid, pg. 409 – 410.

<sup>10</sup> Jonathan Gershuny, *After Industrial Society? The Emerging Self – service Economy*, The Macmillan Press LTD, 1978, pg. 59.

With respect to the nature of work in changing economies, Gershuny mentions as well the progress and degradation of work<sup>11</sup>. The question that might be asked is whether it is necessary for jobs, respectively occupations to permanently lose some of their value because of technical and organisational developments. Many experts attempted an answer to this question. Firstly, there are opinions according to which due to the increased level of enterprises' automation there will be a drastic decrease of manual and repetitive work. Secondly, another effect of progress will be the wider opportunities of technical education as well as improved qualification of workers operating automated systems.

In his analysis, Gershuny emphasises the changes that took place in the distribution of workers at the level of economic sectors, at the same pace with society development, by making clear that the processes generating these changes are: shifts occurred in the production systems, the altered balance between industries, mutations in household organisation, etc. In other words, the factors responsible for the way in which the occupational field develops might be considered to be the organisational ones, related to labour division and the technical factors represented by innovation and investments in high-tech.

Concluding his considerations Jonathan Gershuny remarks on the fact that the current system of organising and developing economic activities has also some problems. One of the issues is represented by the *surfacing of unemployment* to a larger extent than in previous periods within the *tertiary sector*. Another aspect is the *insulation* to which households are exposed, these being the centrepiece of output and consumption. The reason for this insulation originates in the fact that once the *self-servicing of households* is increasingly satisfying these become less sociable.

### **Developments in measuring and forecasting unemployment**

The experts appreciate that the employment rate is a variable category in time. Based on the studies in the field, Y. Barou and J. Rigaudiat have determined that when the level of employment decreases by one unit it does not immediately imply that unemployment will be by one unit higher<sup>12</sup>. Also, if on the labour market a new job is created this does not mean, implicitly that unemployment would diminish by one unit as well.

Official unemployment is computed as difference between active population and employed population, but this way of computing is simplistic and does not pinpoint the actual situation of the phenomenon. When the intent is to realise a

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<sup>11</sup> Ibid, pg. 114.

<sup>12</sup> Y. Barou, J. Rigaudiat, *Le marche du travail. Structure et fonctionnement*, Hatier, Paris, 1985, after Diana Preda, *Ocuparea forței de muncă și dezvoltarea durabilă*, Ed. Economică, București, 2002, pg. 64 – 65.

forecast about unemployment for short periods of time, the authors suggest using the following relationship:

$$\Delta S = 0.38 \cdot \Delta P_{pa} - 0.38 \cdot \Delta P_{oa} - 0.63 \cdot \Delta P_{oi} - 0.19 \cdot \Delta P_{ot}, \text{ where:}$$

$P_{pa}$  = potentially active population, or labour resources of the country;

$P_{oa}$  = population occupied in agriculture;

$P_{oi}$  = population occupied in industry;

$P_{ot}$  = population occupied in the tertiary sector;

The coefficients of the relationship represent values computed by INSEE for the economy of France. In the model created in this manner, it is considered that unemployment might decrease by a unit in one of the following situations:

1. Created 1 : 0.38 = 2.632 jobs in agriculture;
2. Created 1 : 0.63 = 1.587 jobs in industry;
3. Created 1 : 0.19 = 5.263 jobs in the tertiary sector.

It is appreciated that the analysis is valid also in reverse sense, respectively, unemployment might increase by a unit if in agriculture are lost 2.632 jobs, in industry 1.587 and in the tertiary sector 5.263. If the number of jobs is constant, then unemployment increases/decreases by one unit if the labour resources increase/decrease by 2.632 potentially active persons.

The presented model has the advantage of allowing for a more rigorous estimation of unemployment situation on a short period of time, and as result also for the adjustment of policies for the labour market, even if just under the form of some surface corrections. Unfortunately, the authors do not present the ways in which the coefficients could be adjusted, so as to be used in circumstances of swift changes of the economic conditions. Furthermore, considering the quick changes that the world economy is undergoing at present, the model could be used for realising some realistic forecasts about the evolution of unemployment for medium- and long periods of time.

### **The relationship between current conditions of employment and job-satisfaction**

In the last decades, various opinions took shape regarding the influence of the conditions in which employment is realised on the satisfaction of workers during the work process. C.T. Whelan presents, to this end, the occupational stratification and the influence exerted by it on the way of estimating the developed activity. For instance, the Hall-Jones scale of occupational prestige contains the following types of occupational stratification<sup>13</sup>:

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<sup>13</sup> Christopher T. Whelan, *Employment Conditions and Job Satisfaction: The Distribution, Perception and Evaluation of Job Rewards*, The Economic and Social Research Institute, Dublin, 1980, pg. 1.

1. Occupations in various fields of expertise, administrative and managerial placed on superior hierarchical levels;
2. Occupations in various fields of expertise, administrative and managerial on inferior hierarchical levels;
3. Occupations regarding inspection, supervision and other non-manual activities at superior level;
4. Occupations regarding inspection, supervision and other non-manual activities at superior level;
5. Non-manual routine occupations;
6. Skilled manual occupations;
7. Semi-skilled manual occupations;
8. Unskilled manual occupations.

Among these categories there are significant differences with respect to the level of weekly incomes, starting from differentiations between manual skilled workers and workers delivering non-manual, routine activities. This aspect is used as argument for the fact that social classes and strata are regarded as separate dimensions of the occupational stratification.

Whelan approaches the issue of the influence of the occupational stratification on equity estimation, as well, indicating that the two individuals,  $x$  and  $y$  are equitably assessed if the following equality is complied with<sup>14</sup>:

$$\frac{V_x}{I_x} = \frac{V_y}{I_y}, \text{ where:}$$

$V_x$  = the reward given to  $x$  for developed activity at the workplace;

$V_y$  = the reward given to  $y$  for the activity developed at the workplace;

$I_x$  = education level, experience, intelligence and training of  $x$ ;

$I_y$  = education level, experience, intelligence and training of  $y$ .

The necessary observation would be that the assessment of the two individuals should be made in the situation in which the rewards originate from the same source. The equitable perception regarding performances' assessment is defined by the perception of equality between the rates of the rewards for each of the individuals.

Whelan shows that the way in which a full-time employee might achieve job satisfaction is closely related to the following set of occupational rewards:

- wage;
- attractiveness of developed activity;
- job safety;
- decisional freedom about the way in which a job task is realised;
- promotion chances, etc.

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<sup>14</sup> Ibid, pg. 13.

Nevertheless, in assessing occupational rewards following considerations should be taken into account<sup>15</sup>:

- the relationships established between the assessments and the system of occupational stratification;
- distribution of wage bonuses;
- creation of distinct socio-economic groups;
- way in which distribution of rewards is perceived;
- the degree to which the employees identify themselves as members of a socio-economic group.

This approach regards the occupational field rather from a social and psychological perspective, and less from an economic one, without representing a true complex theory about employment and unemployment at the present stage of economic development.

### **The relationship between labour mobility and the field of employment**

Labour force mobility, or its migration generally takes place, as a rule, as result of the wish of individuals to gain a higher standard of living and social status. The unprecedented intensification of the labour force freedom of movement, as one of the effects generated by globalisation, triggers also mutations in the occupational-professional field at national and international level<sup>16</sup>. In order to assess this phenomenon, there are various models that can be used.

One of the models is the *Nakosten and Zimmer Model* which represents the way of assessing the benefits of migration<sup>17</sup>.  $M^* = c \cdot w + u$ , where  $M^*$  = marginal benefit of the migration decision, and  $c \cdot w + u$  = model of the index function which is reached by comparing the wage from the old job ( $Y_0$ ) with the wage obtained in the new job ( $Y_n$ ), as follows:

$$Y_0 = b_0 \cdot x_0 + e_0, Y_n = b_n \cdot x_n + e_n, \text{ iar } c = a \cdot z + v,$$

Which makes that  $M^* = Y_n - Y_0 - c$ , equivalent with the first relationship.

According to this type of model, among the reasons generating labour migration could be mentioned the incomes' levels and the degree of labour force employment in the host and origin country. Next to these reasons, there should be mentioned the intensity of the migration phenomenon in the two countries, the

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<sup>15</sup> Ibid, pg. 17 – 19.

<sup>16</sup> Steliana Perț, Valentina Vasile, Florin – Marius Pavelescu, Liviu Vasile, *Circulația forței de muncă. Scenarii. Posibile evoluții*, în *Probleme economice*, vol. 102 – 103, CIDE, Bucharest, 2004, pg. 30.

<sup>17</sup> R. Nakosten, M. Zimmer, *Migration and Income*, Southern Economic Journal, no. 46, 1980, after Steliana Perț ș.a., Op. cit., pag. 31.

mobility degree of the labour force between the borders of the countries analysed, the way of complying with the human rights and the fundamental rights of individuals, the general level of culture and education, etc.

**The Ferting and Schimid Model** is used for estimating the external migration between two countries<sup>18</sup>. The suggested equation for estimating the migration level is:

$$m_t = a + \sum_k b_k \cdot x_k + c \cdot m_{t-1} + e_t, \text{ where:}$$

- $m_t$  = migration level in year  $t$ ;
- $m_{t-1}$  = migration level of the previous year;
- $x_k$  = *dummy*-type explicative variables, for instance the level of knowing the language of the host country, the way in which immigration issue is handled in the respective country, the existence of common borders, compliance with human rights, etc.;
- $a, b_k, c$  = index type parameters, that should be supervised/estimated;
- $c$  = parameter estimating the dynamics of the migration phenomenon and which might have different values;
  - $c > 1$  indicates that the migration phenomenon increased for the analysed period;
  - $c < 1$  indicates that the migration phenomenon decreased for the analysed period;
  - $c = 1$  shows that the migration phenomenon was stationary for the analysed period.

**The Hatton Model** was conceived in order to bring corrections to a certain extent to the estimation errors of the labour force migration phenomenon starting from the current and preceding values of the explicative variables ( $x_k$ )<sup>19</sup>.

$$\Delta m_{h,t} = b_1 \Delta \ln \left( \frac{S_d}{S_0} \right)_t + b_2 \Delta \ln(e_d)_t + b_3 \Delta \ln(e_o)_t + b_4 \ln \left( \frac{S_d}{S_0} \right)_{t-1} + b_5 \ln(e_d)_{t-1} + b_6 \ln(e_o)_{t-1} + b_7 m_{h,t-1}$$

where:

- $\ln$  = natural logarithm of the considered indicator;
- $(e_d)_{t/t-1}$  = employment rate in the host country for the current year ( $t$ ) / preceding year ( $t-1$ );
- $(e_o)_{t/t-1}$  = employment rate in the origin country for the current year ( $t$ ) / preceding year ( $t-1$ );

<sup>18</sup> M. Fertig, Ch. Schimid, *Aggregate Level Migration. Studies as a Tool for Forecasting Future Migration Streams*, European Commission, Brussels, 2000, after Steliana Perç et al., Op. cit., pg. 32.

<sup>19</sup> T. J. Hatton, *A Model of UK Emigration 1870 – 1913*, The Review of Economics and Statistics, 1995, after Steliana Perç et al., Op. cit., pg. 32 – 33.

- $S_d$  = average wage in the host country;
- $S_0$  = average wage in the origin country;
- $m_{h, t / t-1}$  = migration rate in the origin country for the current year ( $t$ ) / preceding year ( $t-1$ ), calculated as relationship between the migrant stock and total population for the year taken into consideration.

As it can be seen, in this model were considered the following influence factors on the migration model:

1. level of wages in the two countries;
2. employment level degree that can be a favourable or hindering element for finding a job;
3. unemployment rate comparison between the two countries, from which the one in the host country has a higher influence.

As a conclusion, the models that might be used for assessing labour migration highlight the strong links between this phenomenon and the state of the world labour market, but also of the national labour markets for the current period, but also for the preceding ones. Employment and unemployment are two essential components of the labour market that influence to a high extent, if not decisively the mobility of labour resources, as it is also dependent on this phenomenon, more so as economic activities become increasingly global and the knowledge-based society dominant.

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**THE CONSEQUENCES OF GLOBAL FINANCIAL CRISIS OVER  
EUROPEAN UNION BUDGET**

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**Abstract**

*Today the global economy is facing the biggest financial crisis of the last eighty years, with huge implications in real economy. The international financial institutions, together with the developed countries' governments have to take a series of exceptional decisions, decisions meant to minimize the devastating effects of this crisis over the economy and citizens. The European Union Budget is the most important tool of the Community that can decide the amount of revenues and expenditures for each political objective. In this paper will try to capture the main effects that this financial crisis has over the European Budget. The focus will be on the "social policy" expenditures and on the dynamic changes of the budget's indicators.*

Keywords : European Union budget, financial crisis, European Union policy  
JEL classification: F36, G01, H77

**Introduction**

Global financial markets are in a troubled period, with record volatility registered on capital markets, unprecedented losses in financial institutions and the entire banking system shaken from the bottom. The financial crisis that began in the United States has made numerous damages even in Europe. Many EU countries have been forced to take exceptional emergency measures in order to support financial institutions in difficulty.

In order to contain the influences of the current financial crisis on the Community budget first will be to analyze the string of events that culminated with the global financial crisis.

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Millions of Americans borrowed money using the new cheap loans, attracted by the brokers who in pursuit of profit would be lent to anyone for the sake of winning. American citizens have been attracted by their dream house, purchased by real estate loans, which have become increasingly cheap. When U.S. financial markets began to fall the ones fond of cheap houses and financial speculation have vanished, sending the market into chaos. One of the climax of the crisis was on 9 August 2007, when the short-term loan's market simply frozen.

French bank BNP Paribas has decided to suspend three of its investment funds, affected by the exposure they had on the U.S. market. The French were the first who realized the impending crisis and pulled the alarm signal, and the next few months big names from the world bank has admitted that they have problems with subprime loans.

Measures were taken to this end for banks' activities to return to normal. For example, the European Central Bank has invested 95 billion, the Federal Reserve System (FED) and Bank of Japan took similar measures, but commercial banks have allegedly increased risk premiums, which led to a rapidly increasing interest rates.

The first serious problem in the European Union area has emerged in Britain in August 2007 when the largest provider of mortgages, Northern Rock, started to crash.

European Union leaders have committed to coordinate national efforts to support the banking system, to protect depositors and to increase the credit's flows. Under the plan, governments would have to buy shares in banks to help them consolidate their finances and guarantee, temporarily, the banks refinancing system in order to reduce credit crisis and boost the economy. While increasing confidence in the financial system European governments have also pledged to guarantee interbank loans and were also willing to guarantee new loans for maximum 5 years.

In this respect, European leaders in the summit's emergency meeting in Paris have developed a common plan to face financial crisis. In this joint action plan were references to a number of possible solutions out of crisis, such as:

- Taking a firm commitment to act together in a decisive way, in order to restore confidence and proper functioning of the financial system;
- All Member States must take decisive action and use all available tools to support institutions involved in enhancing the efficiency of adoption of appropriate measures for the present situation;
- European Central Bank and many central banks have taken the decision to reduce interest rates in order to boost lending.

Implementation of these measures require the European Union, Euro area governments, central banks and supervisory authorities to have a unified and coordinated approach, with the priority objectives to ensure adequate liquidity for

financial institutions, facilitating the financing of banks, providing a sufficient level of flexibility in the implementation of accounting rules and taking into account the circumstances and procedures for improving cooperation between European countries.

In reality, it was proved that all these measures, each of them, have failed to stop financial crisis advancing march and its propagation in the real economy.

In a new attempt to limit the effects of the crisis was determined again a concerted intervention of all European countries and the most important European Union institutions. The main lever through which the EU can intervene in the economy of European countries as its budget and the full range of measures envisaged in was reflected in 2 the 2008 budget and particularly that for 2009.

### **The operating mechanism of european union budget**

The operating mechanisms of the European Union budget are complex and intelligible to very few. Budgetary resources are far from being sufficiently transparent that the common tax payer can understand, and making decisions on spending is usually left up to those directly involved, such as the Budget Committees of the European Parliament and the Council of Ministers. Those who understand this complicated bureaucratic mechanism are generally specialized in this subject and that is the main reason for usually positive reports on the EU budget.

Although representing only a small fraction of total national income of EU member countries, the European budget is an important tool in the transmission of common political goals. The budget is used to finance a wide range of activities in the Member States, for example in agriculture and rural development, infrastructure construction, education and research, human resources and social policy, environmental protection. The budget also covers costs of administration of the Community institutions and a part of the European budget is used for the cooperation development and humanitarian aid granted to third countries.

The European Union budget is an instrument that determines the level of expenditures that can be made in each of the areas of Community policy, and the projected revenues to be collected to finance that year spending.

Being the most important tool that influences the amount of all expenditures and revenues of the political goals, the European Union budget can not be compared with a national budget because it has some unique defining characteristics. For example, in the decision making process, the European Union must comply with the principles and make compromises between different states, particularly if the expenditure regards agriculture and regional development.

In addition, the Community budget differ from those of international bodies, budgets which are financed from contributions of Member States, because the

main objective of the European Union is to strengthen integration. Given this goal, the EU budget function and work is carried out by specific rules.

In the early years of the European Economic Community, the main purpose of the budget (which at that time was based on transfers from the Member States) was to finance the Common Agricultural Policy (CAP). The 1971 reform created the concept of own resources that consist of customs duties applied to goods imported from outside the Community and agricultural duties levied on imports into the EEC, directed to the European budget. While PAC costs have increased from 1970, the Community has received new features, so new areas of interest to support regional development and thus too have increased costs, and the two own "traditional" resources were no longer able to cover expenditures, necessitating additional payments of the Member States. Consequently, a third source of funding was therefore introduced in 1979 consisting in a small percentages of the amounts collected through the Value Added Tax collected by each Member State.

While the costs of Common Agricultural Policy could not be controlled and traditional own resources have continued to decline, the latter were soon proved insufficient. Accordingly, in June 1988, the European Council in Brussels has introduced a new own resource computed from own gross national product (GNP) of each Member State. It was also determined an upper limit of own resources which may be required to finance the expenditure as a percentage of the GNP of each Member State.

Agreement closed in Edinburgh in December 1992 increased the limit to 1.27% of Europe Union GNP, while making the first steps towards a further decrease of the importance of the VAT. This agreement came into force in early 1995.

In 1999, the Berlin European Council asked the Commission to prepare a new decision on own resources, which should provide adequate resources for the 2000-2006 period while respecting budgetary discipline structure. The new system was to be "fair, transparent, cost-effective and simple, being based on criteria that best reflects the ability of Member States to finance the European Union.

The European Union has a number of unique features that bring a strong influence on potential budgetary reforms. The level of centralization differs greatly from other political systems in which the government tends to be the main actor on the public finances stage. To view the subject from another perspective, you should know for example that the American Federal Government spends approximately 20% of the GDP of the United States or 20 times more than at the European level. It is clear, the perfect differences between central government and sub-national level in the budget operating mode, and so it is clear that this is not the model applied by the European budget. At European level there is also an obligation to balance the budget and expenditures are limited to a fairly rigid environment by imposing a long-term framework.

Three distinct types of governance characterize what the European Union is today. It is primarily involved in highly regulated activities, in the broadest sense of the word: traditional Community method of using powerful legal instruments (directives, regulations) is the center of its work. Secondly, the EU is a budget authority, although its influence in this area is very limited. It is clear that the European Union role in European Governance is more to regulate than to engage in financing policies. Indeed, it would not be hard to anyone to imagine a Union that would not have any role in determining public expenditures other than to cover their administration costs. Third, and ever more in present times, the EU has become a coordinating body for national policies. This type of coordination occurs in a wide range of processes, some of which (the Pact of Stability and Growth) is treaty based while others have a more intergovernmental nature. Lisbon strategy, clearly original, was part of the latter category, but its release showed an assimilation of the coordination process based on treaties and other elements of regulatory activity.

Initially, to obtain the European Union budget, it is necessary to pen a preliminary budget, taking into account the needs of the EU's policy and its priorities for the next period. This plan is sent to the Council and take this fine plan, and now becomes a "draft budget". In the next phase, this „draft budget” is sent to the European Parliament whose power depends on the nature of expenditure. If the expenditures are classified as mandatory, the European Parliament only proposes the amendments and the Council has the power to determine the final amounts while for optional expenditures, the Parliament is the one who sets the budget. After two readings of each institution, the European Parliament is the one that adopts the final budget and the President of the Parliament signs it. Since that time, the European Budget appears and can not be attacked by any institution.

The budget debate was hard which is not surprising given the long list of topics contradictory. European Union budget is subject to inter-governmental negotiations, and often the subject of bargains, so it is rather a reflection of political preferences and historical compromises than a tool for maximizing welfare. The EU is faced with conducting the ambitious "Lisbon Agenda" which was opened in 2000 to create the most competitive economy "by 2010". These two problems have put two of the largest programs under budget spotlight: the Common Agricultural Policy and Structural Funds (SF), which together consume 80% of the EU budget.

Often, when the question of benefits and advantages arising of achieving the status of European Union member, money are the only ones that matters. Politicians assure there siblings that they attempt "to obtain the maximum" of the EU budget. What seems to be important is not economic and political stability in Europe, but rather balance the budget problem. Those who get more money back from the Community defeat in this competition. Sometimes you have the

impression that the main desire of each country is to become a net recipient of European funds.

The advantages of being an European Union member state should not be measured in money, however, is quite interesting to see how much actually the European Union costs and how the money are spent. EU funds do not disappear somewhere in the bureaucracy in Brussels. But rather, nearly 85% of all money spent by the Union are in the States. For these amounts can be clearly identified which Member State takes money, what amount, for what part of its population, for which policy area and for which action.

The European Union budget is characterized by an important function of redistribution, the transfer of funds from richer regions to poorer ones in order to obtain convergence (structural policy).

The present budget of the European Union has long ceased to represent the priorities of European policy, being the result of decisions taken decades ago and of continuing growth adjusting decided under pressure of external events or for policy expansion. Increasing remoteness of initial needs and priorities of political support undermines the public opinion. EU Budget is ancient and is not caching the current needs of the Community and should be reformed by rethinking the basic procedures of taking decisions.

The budgetary balance sheet, clearly, do not show the whole picture of belonging to the European Union. The budget has its shortcomings and inconsistencies, however, a closer look to the EU budget will show how the public view on Community costs is not always consistent with the facts.

The European Union budget is designed through 3 elements. The financial perspective sets the parameters to be fit for EU spending for a seven years period. Own Resources Decision determines the maximum amount and type of income of the Community budget. The third element, the annual budget remains within the limits set by the first two elements, approve budget's funds and defines the way in which they are to be allocated to individual areas.

At this time the European Union budget is financed by 3 categories of income. Traditional own resources (TOR) which consist of customs duties applied to goods imported from third countries, the agricultural tax and sugar leaves. Resources taken from the Value Added Tax (VAT) are calculated applying a percentage rates on uneven income of the harmonized VAT of each Member State. The biggest source of revenue (almost 70%) comes from the Member States' contributions calculated as a percentage of the Gross National Income (GNI). This source is defined as a source which balance the budget, i.e. the difference between expenses and other income sources. Percentage of GNI due by each Member State is computed ex-post as the difference between expenditure and income, revenues from the traditional resources and VAT. This residual value is divided between Member States in proportion equal to the amount they hold in the European Union total GNI, and is paid by each Member State from the

national budget. In 2006, for example, before the start of the financial crisis represented almost 65% of total revenues.

On one hand, all countries are obsessed by limiting their contribution to the budget, and on the other hand, no country seems ready to give up their agenda of projects' spending. Most of the resources are transferred to the European Union budget from the national budget - which apparently violates the Treaty on own resources - and the Member States are trading division of funds between them, funds for expenditure on agriculture and structural funds, in order to obtain a net balance in their favor. National interest is limited to what is going to pay from the national wealth and what will the farmers and it's regions receive.

Today the European Union consists in two very different activities: first, reallocation of resources between Member States on the other hand, production through common policies and institutions of European "public goods". While extensive areas meet common goals, redistribution varies quite a lot, conceptually and analytically, from the actual production of "public goods" such as free movement of people, internal security or safety and plant health, "public goods" belonging to the allocating function the public budget as defined by Musgrave.

Redistribution is motivated more by considerations of justice and equality, then by an optimal allocation of resources to meet collective demand. At the European level the main redistributive programs are the allocation of Regional, Structural and Social Funds, including the use of structural funds of Commune Agricultural Policy (CAP) and Fisheries Policy and other issues. The main goal of these programs is to reduce income disparities within the Union and to foster economic convergence of poorer regions.

Another feature of expenditures redistribution which justify their separation is that they are managed by Member States and their regions everything under the direct control and guidance of the European Commission, rather than by the Commission directly.

The conflict generated by obtaining positive net balance for each Member State has become an impediment of the budget creation consistent with policy priorities today. Net positive taxpayers vote against any increases in resources since they fear that they will bear unequal burdens; program's beneficiaries on the other hand are voting against any loss of existing funds. As a result, the possibilities of diverting to new priorities are very small.

Hard negotiations over the net positive balance led to the proliferation of such clauses granting special treatment of some Member States, both in terms of revenues and expenses. Great Britain discount - equal to two thirds of ex-ante deficit - led for years to grant discounts for other countries (Austria, Germany, Netherlands and Sweden achieved reductions in financing these funds, together with reductions of VAT's percentage contributions; two of them are granted small contributions to GNI's resources). Total result, however, does not seem fair: countries with similar levels of economic development (prosperity) face net

payments and received funds quite different. As a result, not only the budget has become increasingly opaque, but its legitimacy has been questioned ever more.

Serious changes in the budget can not be done until the problem of the net positive balances is resolved; any solution can be based on a generalized correction mechanism that will not only align the net balance automatically based on preset criteria, but will also treat all creditor Member States equal.

The ministers of finance of the European Union that have tried to coordinate and consolidate the budget according to the national tax incentives have brought government deficits to recession.

### **European union budget and main indicators 2007-2009**

Severely hit by the biggest financial crisis since the Great Depression of 1930, the European Union economy plunge into a deep and reiterated recession, forcing governments to spend millions of Euros to stimulate economic growth.

While on the one hand, public expenditure increased to much, revenue from taxes decreased, and governments of the EU Member States were forced to pill up deficits.

Based on the European Commission evaluation, the average deficit in Member States this year is more than double, i.e. 4.5%, compared to the level calculated for 2008 of 2%.

In 2008, for the first time, most of the European Union budget (45%) was directed to measures that will lead to economic growth and measures that will lead to a greater cohesion in the EU. Agriculture continued to receive over 40% of the European funds.

Twelve of the 27 EU member states will reach budget deficits above 3% of Gross Domestic Product (GDP), the maximum allowed by the European Union rules in normal times.

Ministers of finance from the European Union said that while short-term budget deficit will increase, many Member States will remain strongly committed to long-term compliance with the principles of sound and sustainable public finances.

The ease adopting of this year's draft budget shows the Council determination to support the proper use of public Community funds and to respond to concerns of European citizens, whether they agree to support growth and competitiveness, policies favoring Member States that have joined the EU in 2004 and 2007, or the solidarity between the European Union and third countries.

In turn, the European Parliament have expressed support, although a little cautious, for the compromise reached with the Council regarding the 2009 European budget. This budget forecast payments for certain actions at a very low historical levels, including the ones made from the financial perspective.

However, European Parliament will remain attentive at the finance of needs, which in it's opinion, would seem necessary during the budgetary year. Mean time, Parliament does not want to compromise on the financial assistance for agricultural production in developing countries. The European Budget in 2009, indeed, disclose budget facilities of 1.8 billion Euros, spread over a period of 3 years, to help agricultural production in developing countries that were affected by rising prices of food, the Council accepting to use flexible instruments, till a upper limit of 420 million, as requested by the European Parliament. Despite the growing public demand for increased involvement in education, research and infrastructure, this expenditures have reached only one third of the costs opposite to those more than 40% of total expenditure on agriculture - the sector in decline.

Moreover, there is a growing demand for a greater emphasis on common policies such as foreign policy, defense, security, immigration and civil rights, and yet these areas are neglected.

Overall EU budget for 2009 will be approximately 116.09 billion Euro in the form of payment appropriations (0.89% of EU GDP) and approximately 133 billion Euro in commitment appropriations. This amount corresponds to an increase of 2.5% over 2008 and represents 1.03% of the total General National Income of the Community.

In the current economic climate, complementary objectives of competitiveness and cohesion for economic growth and employment should be strongly supported, and most of the budget that is about 45% or 60.2 billion Euros will be devoted to these goals.

### **The EU Budget between 2007-2009 – financial framework (aggregate)**

#### *Million Euro (current prices)*

<b>Indicators</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
<b>1.Suistanable growth, from which:</b>	<b>60.195,88</b>	<b>58.337,95</b>	<b>54.854,33</b>
Competitiveness for growth and employment	11.769,00	11.082,00	9.367,55
Cohesion for growth and employment	48.426,88	47.255,95	45.486,78
<b>2.Preservation and management of natural resources, from which</b>	<b>56.121,44</b>	<b>55.559,71</b>	<b>55.850,23</b>
Market related expenditure and direct payments	41.131,36	41.006,49	42.311,66
<b>3.Citizenship, freedom, security and justice, from witch</b>	<b>1.514,89</b>	<b>1.634,91</b>	<b>1.443,63</b>
Freedom, security and justice	863,93	731,77	623,83
Citizenship	650,96	903,14	819,80
<b>4.UE as a global player</b>	<b>8.103,93</b>	<b>7.551,22</b>	<b>6.812,46</b>

<b>5.Administration</b>	<b>7.700,73</b>	<b>7.279,21</b>	<b>6.977,86</b>
<b>6.Compensation</b>	<b>209,11</b>	<b>206,64</b>	<b>444,65</b>
<b>TOTAL</b>	<b>133.845,98</b>	<b>130.569,64</b>	<b>126.383,16</b>

Competitiveness will be boosted by an increased support for the *research* framework program (+ 10.9%), the **competitiveness and innovation** framework program (+ 22.2%) and **lifelong learning** (+ 6.5%). Expenditure on structural and cohesion policy amounts to 48.4 billion Euro, according to the 2009 budget of the European Union.

In addition to promoting economic development and protecting natural resources, the European Union also seeks to meet the concerns of citizens in the area of freedom, security and justice. In the 2009 budget will be available for this purpose 863.9 million Euros and an additional amount of 651.0 million Euros was allocated for programs in the citizenship field, such as support for youth and culture. EU will maintain a central role as a global player, the budget for external actions increased by 7.3%, up to the amount of 8,1 billion Euro.

Administration costs related to all EU institutions amount to 7.7 billion euros. As regards the Commission, the European budget for 2009 provides the latest installment of the 250 new posts following the accession of Bulgaria and Romania in 2007.

It also notes an increase in some of the commitments on policy, such as:

- For the "Enterprise" from 510 million Euro in 2007 to 663.24 million Euro in 2008, a relative increase of 30%, which shows a growing interest of the European Union in encouraging the economy;
- For the "Energy and transport" from 1808.90 million Euro in 2007 to 2739.98 in 2009, i.e. 51%;
- or the "Research" from 3574.75 million Euro to 4071.76 million Euro, or approximately a 14% increase which should spur economic development through new discoveries or improvements in productive and economic processes.

### **Appropriations for commitments (selection on policy fields)**

**Millions Euros**

<b>Indicators</b>	<b>2009</b>	<b>2008</b>	<b>2007</b>
1.Economic and financial affairs	441,90	398,48	494,94
2.Enterprise	663,24	596,51	510,03
3.Energy and transport	2.739,98	2.806,85	1.808,90
4.Research	4664,91	4.050,70	3.564,67
5.External relations	4.071.76	3.973,46	3.574,75
<b>TOTAL appropriations for commitments</b>	<b>130.997,83</b>	<b>127.896,12</b>	<b>126.383,16</b>

## Conclusions

Examining the European budget we could see some of the effects of financial crisis over it:

- There is an increasing number of *reviews* of the financial perspective (it started with Galileo in 2007, continued with the food facility in 2008, and now the plan to revitalize the economy - projects for which the financial perspective has changed in 2007-2013 although institutional agreement between Parliament, Council and Commission prohibited this);

- First steps towards the creation of a *European public debt instrument* supported by Hungary and Latvia were made (Romania and Lithuania are following), supporting guaranteed by the Community budget. There are policy-makers that are already taking into consideration the Eurobonds;

- It had reinforced the impression that there are too many resources in Chapter 2 (Agriculture). From the perspective of countries like Romania, whose net beneficiary status depends largely on the access to resources in Chapter 2 and 1b (Cohesion for growth and employment), we are dealing with a negative trend. It is possible that major contributors to the Community budget to demand less generous allocation for agriculture in the near future.

The budgetary discipline of the community tends to be loosen as a result of the financial crisis. Financial perspective loses the role of firm framework in financing the Community; the tendency is to create a public debt instrument that will weaken the dependence of the institutions over direct funding from Member States.

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**BUSINESS CYCLE SYNCHRONIZATION IN MONETARY UNION**

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**Abstract**

*The purpose of this paper is to examine the self-enforcing nature of business cycle synchronisation in the process of monetary integration. Application of value added concept for description of business cycle and as a indicator of total economic activity is also discussed in the paper.*

**Keywords:** monetary integration, business cycle, GDR, GDP

**JEL-codes:** E22, E32, F36

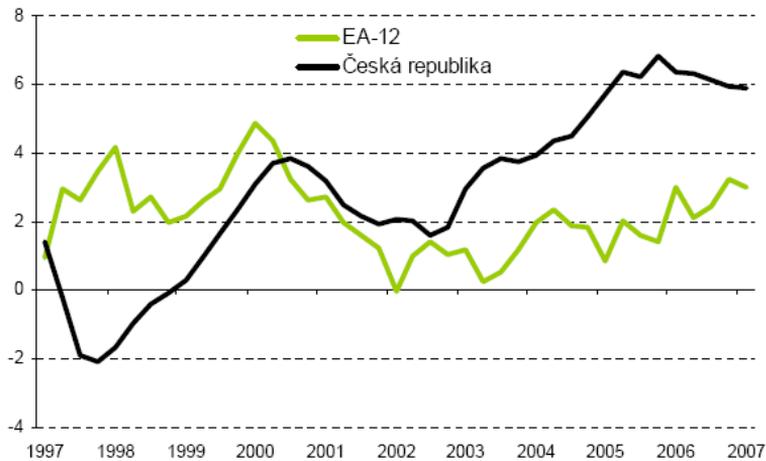
**1. Introduction**

Cyclical development in the economic activity is an important argument in discussions about monetary integration. Expedience of monetary integration is derived from the synchronization of business cycle described by development of widely used indicator - the GDP. Following graph shows the cyclical movement of GDP in the Czech Republic and twelve countries of eurozone (EA-12). As it can be seen here, there exists an asynchronous cyclical development, hence it is said that membership in the European Monetary Zone is not suitable for the Czech Republic.

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**Chart 1: Business cycle in the countries of EA-12 and in the Czech Republic (year-to-year changes of GDP in %)**



**Source: Analysis of harmonization, CNB**

The approach mentioned above raises many questions. First of all, is GDP the best tool for business cycle description?<sup>20</sup> If the answer is negative then another question follows: How should we record such a business cycle? Construction and computation of a more appropriate indicator for business cycle description is question under debate in this paper. The aim of this paper is also to find an answer to a related question - whether business cycle synchronization is a self-enforced feature of monetary integration<sup>21</sup>.

### **GDP and economic theory**

Widely used indicator GDP is treated as an integral part of modern macroeconomics, in addition to that GDP is said to be crucial guideline for economic policy. GDP is defined as a sum of value added by each firm, government institution and productive households<sup>22</sup> and is in the centre of the system of national accounts. Dynamic development in the case of GDP computation and national accounts as a whole dates back to the fourth decade of the 20th century in connection with rising demand of politicians for statistical data describing the development of economic systems. A substantial contribution to

<sup>20</sup> Business cycle is usually defined as deviations of real gross national product (GNP) from trend and trend is defined as steady state in the sense of growth of output per capita, consumption, investments, etc. corresponding to growth of technology. See Kydland, Prescott [1990] For purpose of this analysis, there is no need to differentiate between GNP and GDP.

<sup>21</sup> If it is this case, it is meaningless to wait for synchronization in the course of GDP.

<sup>22</sup> Looking at GDP from a different angle, GDP is the monetary amount that forms the incomes that are distributed, redistributed, consumed or saved. See Understanding National Accounts, str. 17.

the elaboration of the system of national accounts was brought by Simon Kuznets. This economist is strongly connected with so-called „Keynesian revolution“, hence, it is not surprising that the national accounts are based on methodological fundamentals of Keynesianism<sup>23</sup>.

### *Production*

Production is the cornerstone of the system of national accounts. This item covers all goods and services produced in an economy within given period intended for final consumption, intermediate consumption or for export. According to classical economics<sup>24</sup>, annual production can be used in two ways - for production or for consumption.<sup>25</sup> Larger part of production is intended for production purposes, for renewal of capital, reserves, or for capital widening. Thank to accumulation of capital, process of capital widening leads to increasing production in following periods. The remaining part of annual production is used for consumption purposes<sup>26</sup>.

By this two alternative uses is annual production fully exhausted. Naturally, the more is intended for consumption purposes, the less can be used for production purposes, and *vice versa*. Relation between consumption and investment is aptly expressed by Röpke<sup>27</sup>:

*„The formation of real capital (investments) must be balanced by a restriction of consumption, ..., the inference is: that the proportion between consumption and real-capital formation cannot be changed at will without causing disturbances.“*

A restriction of consumption will enable creation of savings that are used for purchase of capital goods, in other words, savings are necessary for capital widening and subsequent rise of production. Because savings are spent on production purposes, there are no outflows of monetary units (savings) from economic system. These funds (savings) are unlike consumption expenses spent on the production purposes in the sphere of capital goods. Hence, savings have an

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<sup>23</sup> First of all, the connection between keynesianism and national accounts is the concept of value added as a basis for description of economic performance. This concept is said to avoid so-called „error of double-counting“. Another linkage is also its emphasis on consumption, narrow definition of productive activities, net values, etc.

<sup>24</sup> Adam Smith or James Mill.

<sup>25</sup> Smith [1904]

<sup>26</sup> Mill [1808]

<sup>27</sup> Röpke [1936], p. 99

impact on demand for capital goods. This fact was formulated by Adam Smith as a so-called „saving-is-spending“ theorem.<sup>28</sup>

Classical economics tells us that we have to save a part of an annual production for production purposes to enable future consumption to increase. As Röpke notes, decrease of consumption can be only relative, consumption and productive expenditure can grow simultaneously, because of growth of total production<sup>29</sup>. Let us compare this theoretical relation with data provided by the system of national accounts. Total production is the basic item of this system and is recorded in the production account. Capital account provides information about the amount of capital expenditures within given period according to the methodology of the national accounts (so-called „gross capital formation“).

Following table shows overview of changes in the rate of growth in capital expenditures and production (both items are recorded in current prices). In year 1998, the rate of growth of production decreased by almost 2 percentage points, this development in production was preceded by 21 percentage points slump in capital expenditure in the previous year. The same is true for year 2002. These years can be considered to be in accord with logical relation between investments and production.

**Table 1: Changes in rate of growth of production a investments, Czech republic, 1998-2007**

	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Production	-1,97	-6,25	7,51	-0,88	-6,49	3,13	4,71	-3,92	6,5	-2,3
Investments (t-1)	-21,42	5,41	-3,27	15,02	-6,74	-6,51	-1,96	11,71	-11,34	12,3

**Source: Czech statistical office, own calculation**

Year 1999 was characterized by a strong fall in the growth of production. But this reduction was preceded by accelerating rate of capital expenditure<sup>30</sup>. This situation has been repeated in years 2001, 2005 and 2007. So, in these four years real development does not agree with theoretical explanation of relation between investments and production. On the contrary, in years 2000, 2003, 2004 and 2006 we can see accelerating growth of production, which was preceded by deceleration in the growth of capital expenditures. Briefly summarized, data are in accordance with theory only for two years of the examined period. So the

<sup>28</sup> What is saved is also consumed, but the consumers of savings are not the consumers in common sense. „That portion which he annually saves, as for the sake of the profit it is immediately employed as a capital, is consumed in the same manner, and nearly in the same time too, but by a different set of people, by labourers, manufacturers, and artificers, who reproduce with a profit the value of their annual consumption. His revenue, we shall suppose, is paid him in money.“ See Smith, Book II, Chapter III.

<sup>29</sup> Röpke [1936], p. 109

<sup>30</sup> Bear in mind that in this case we take investment as gross capital formation. By this item are not covered all expenditures made for the purpose of subsequent consumption.

theoretical relation between investments and production seems to be very weak in the case of Czech national accounts in this period.

### *Value added*

Undercounting of capital expenditure in the system of national accounts is considered to be the reason for weak connection of investments with production. The logical consequence is that the concept of value-added does not display the real range of economic activity<sup>31</sup> (revenues and expenditures) that creates this value-added. This fact is caused by methodology of GDP computation, i.e. the exclusion of many production expenditures from this indicator which has far-reaching implications.

Let's consider some economic activity creating zero added value. Purchases of inputs (so-called intermediate production) were made and then used in forming production. With the aid of these inputs and factors of production, goods or services are produced and sold on the market. If the producer does not reach the price sufficient to cover production expenses (excluding compensation of employees and other expenses<sup>32</sup>), the result will be zero or even negative added value. This corresponds with the situation of erroneous entrepreneurial presumption about future market data<sup>33</sup>. It is evident that real economic activity was carried out. Many inputs and factors of production were used up in the process of production. But because of the zero added-value, this activity is escaping from the perspective of GDP. Put in different way, this activity does not exist from the GDP's point of view.

The discussion now turns to the question of full coverage of capital expenditures in GDP, i.e. the exclusion of the intermediate consumption, which is a standard practice in the national accounts system. Methodology of GDP understands as an intermediate consumption acquisition of small tangible assets, energy and services consumption, including for example operational leasing of equipments, marketing expenses, storage expenses, etc. All of these expenses are excluded from GDP<sup>34</sup>, even if there are expressions of real economic activity, use

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<sup>31</sup> In general, we can define the economic activity as an endeavor to improve the present living condition in the condition of scarceness. The economic activity is displayed by consumption and (mainly) production.

<sup>32</sup> In the computation of value added (for example in the case of non-financial corporations) is only part of total costs included in the intermediate consumption, whilst in the production are included almost 75 percent of receipts. It is not unusual that the main source of agent incomes are interests, rents, etc. This incomes are not included in the value-added computation. Value added of this subjects can be even negative, while disposable income is usually noticeably positive.

<sup>33</sup> But the methodology of the national accounts in essence doesn't allow the situation of negative value added.

<sup>34</sup> As well as acquisition of estates, licences, etc.

of scarce resources. So, when revenues do not exceed expenditures, GDP tells us that there was no economic activity. But the opposite is true.

### *Consumption and savings*

To record total economic activity, all revenues (expenditures) spend in the economic system within a given period have to be recorded in the indicator of economic activity. But according to mainstream economists, we would make a mistake called „double-counting error“. We should avoid this mistake by excluding intermediate consumption<sup>35</sup>. If the aim of our endeavor is to construct economic indicator showing total added value, this is without any doubt an appropriate approach. But if we want to obtain an indicator of total economic activity, we cannot exclude large part of revenues (expenditures) related to the intensity of usage of scarce resources, i.e. capital goods<sup>36</sup>. Furthermore, there are many transaction not included in production and intermediate consumption at all.

Thus, if we want to detect the fluctuation in total economic activity we cannot put aside majority of transactions. According to classical economics, the focus lies in production, i.e. larger part of annual production is intended for production purposes. „*Consumption in the necessary order of things is the effect of production, not production the effect of consumption.*“<sup>37</sup> But in the case of GDP, almost three quarters of GDP are made by consumption. Dominant position of production expenditures in an economic system is also confirmed by data from the national accounts system. In the case of the Czech Republic, intermediate consumption<sup>38</sup> to production ratio amounts to 60 percent, intermediate consumption to value-added ratio amounts to even greater proportion of 150 percent.

Driving force of economic activity is necessarily production, and not consumption. This follows from the fact that what is available for consumption had to be produced before<sup>39</sup>. Importance of consumption is valid on the level of an individual firm because of the existence of demand for given good or service provided by this firm is necessary condition for the operation of this firm. But on the level of an economic system as a whole, the consumption is fully dependent on the production.<sup>40</sup> Because productive expenditures are a large part of total economic activity, GDP records the turns in the development of total economic activity with delay.

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<sup>35</sup> „To exclude double counting, we will endeavour to include in gross domestic product only final goods and not capital goods that are used in the process of production.“ Samuelson [1995], p. 109.

<sup>36</sup> Reisman [1996]

<sup>37</sup> Reisman [2006], p. 8

<sup>38</sup> Which are only a part of total productive expenditures.

<sup>39</sup> Johnsson [2002]

<sup>40</sup> Reisman [1996], p. 696

Reisman [1996] shows on the base of classical economy the substantial function of savings, i.e. that higher propensity to save results in the growth of investment expenditures enlarging production capacity. Process of production then generates more incomes for factors of production such as a wages, profits, dividends, interests, which are in the next round used for consumption, or saved. This linkage between savings and volume of consumption goods indicates that savings do not ruin production because of decreasing demand, but on the contrary, the existence of savings enables the production of capital goods and then of the consumption goods to increase.

Application of GDP (value-added concept) for description of business cycle seems to be problematic also in other aspects. In the view of GDP a producer does not produce a whole of his product, but only a part of it, i.e. value-added<sup>41</sup>. But in reality, we purchase total product and producer gains the whole of the monetary value of his product, not only a part. If we take into consideration just a profit, or, to be more specific, a part of total profit (production minus intermediate consumption), than we consider total economic activity fluctuation by only a part of total economic activity. Reisman describes the approach of mainstream economists towards error of „double-counting“ as follow: „it is an error to claim that all that is produced, is in fact produced.“<sup>42</sup>

Another problem arises from the definition of productive activity. As Reisman points out the productive activity is „activity the purpose of which is the earning of money.“<sup>43</sup> The methodology of national accounts specifies the production boundary in a narrower sense: productive activities are only those activities creating added value. For example making money on interest differential is not a productive activity in the approach of national accounts methodology. Due to this fact also interests, dividends, rents, etc. are not included in the indicator of total economic activity fluctuation.

As a result, there are many arguments against the application of GDP for description of business cycle. According to the theory, greater part of total expenditures is formed by production expenditure, investments. Consequently, it is appropriate to push forward an emphasis towards investment expenditures, towards production of capital goods which production is subject to more considerable fluctuation. Investment expenditures are most sensitive expenditure to changes of monetary condition and are in the center of cyclical movements<sup>44</sup>. From the above-mentioned reasons, Reisman has constructed an alternative indicator (GDR) which is more suitable for characterization or description of cycles.

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<sup>41</sup> Recall the „double counting error“.

<sup>42</sup> Reisman [1996], p. 677

<sup>43</sup> dtto, p. 443

<sup>44</sup> Röpke [1936]

### 3. GDR

Evolution in the financial sphere of an economy has a significant impact on the real sphere. Volume of credits, stock prices, prices of bonds, interest rate, payment morality, all these „financial“ factors determine desire to save, to invest, to extent a production capacity, to consume. Monetary theory of a business cycle regards a disruption of monetary conditions (equilibrium) as a trigger mechanism of a business cycle.<sup>45</sup> This disruption is characterized especially by artificially low interest rate<sup>46</sup> and excessive credit expansion of fiat money. The result is an artificial rise in revenues, profits<sup>47</sup>, which change entrepreneurs' decisions<sup>48</sup> and allocation of scarce resources. We are caught in the situation called „calculation chaos“, in the world of exaggerated profits and undervalued costs.

The impressions of improved profit and loss statement usually cause increasing economic activity, extension of production capacities. Rising demand for factors of production is followed by rising prices of inputs, capital goods, which in long-term horizon lead to worsening of cost conditions. The reason is restricted supply of capital goods together with unchanged consumers' preferences<sup>49</sup>, the supply of capital goods cannot satisfy demand in the phase of boom. Lack of capital goods and increasing prices of capital goods end the phase of economic boom<sup>50</sup>.

Excessive demand for capital goods is enabled by the expansionary credit emission that can increase credit volume above the amount that would be in accordance with consumers' behavior regarding consumption and savings. To invest into extension of production capacity assumes higher demand of consumers and, simultaneously, resources release from production of consumers' goods, i.e. savings formation which served as a source of investments. Realization of investments without change in preferences is enabled only due to additional issue of new funds (fiat money). Investment carried out by additional money will turn out as bad investments in the future.

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<sup>45</sup> Here we can mention the difference between business fluctuation caused by technological changes, changes in the preferences, etc. (real business cycle) and monetary business cycle caused by changes in the monetary conditions.

<sup>46</sup> To the intent that interest rate set by central bank and natural interest rate generated by real economy. Wicksell [1907]

<sup>47</sup> Increasing amount of money will influence the income side, cost side of the profit and loss statement is influenced by excessive monetary expansion in the second row.

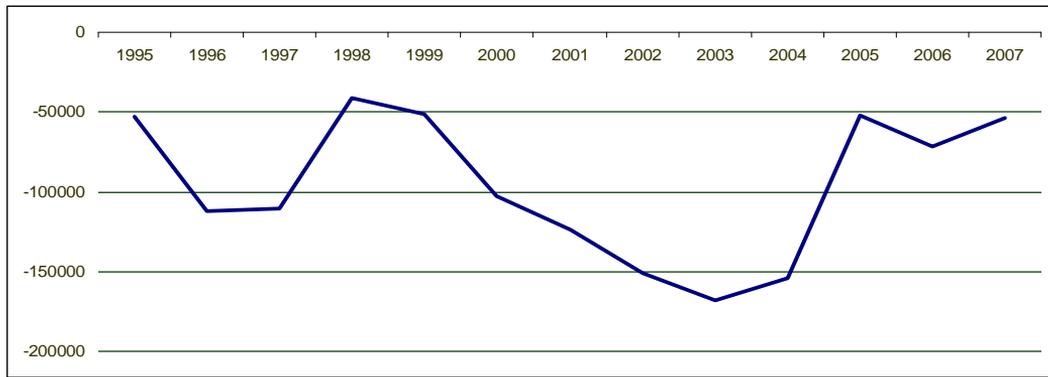
<sup>48</sup> But also consumers.

<sup>49</sup> In other words, there is no transfer of sources from the productions of consumption goods to the productions of capital goods, because consumers didn't change at all or in the sufficient level their preferences. This situation correspond to so-called „enforced savings“, lower real savings that investments.

<sup>50</sup> This development is inevitable, if the investments are financed by expansive monetary policy. Hayek [1935]

Note that investments based on real savings can also turn out to be erroneous, because entrepreneurs make mistakes in their forecasting of future market data. But we examine the situation where a large number of entrepreneurs make bad decisions, so we consider making mistakes in such extent that this cannot be reduced to bad presumption of consumers' preferences<sup>51</sup>. As it will be showed later on, the reasons are rapid changes in money supply creating unstable monetary condition, or put differently - „calculation chaos“<sup>52</sup>. Relation between savings, consumption and investments are shown in the following chart.

**Chart 2: Difference between savings<sup>53</sup> and investments (1995-2007), mil. CZK**



**Source: national accounts (CZSO), Balance of Payment statistics (CNB), own computation**

Chart 2 shows the difference between savings and investments. It is evident that in the case of the CR savings did not reach the level of investments made in the long term, regardless of the phase of the business cycle<sup>54</sup>. The amount of investments is pulled away from the amount of savings. This development is not natural, as Röpke wrote: „...*the capital formation (investment) must be balanced by a restriction of consumption.*“<sup>55</sup> Restriction of consumption is necessary condition for savings formation which amount then restricts the amount of investments.

<sup>51</sup> In the case of consumers it is the matter of bad presumption of real purchasing power.

<sup>52</sup> In general, under the term „calculation“ we understand the decision about the application of scarce resources. As a calculation chaos we understand the situation in which the external conditions leads to broad malinvestments, lowering of production capacities and inability to pay off a credit, because of inappropriate evaluation of costs and revenues.

<sup>53</sup> Savings are calculated as a sum of savings generated by domestic economy (S.1) and inflow of foreign sources (financial accounts of balance of payments, exclude financial derivatives).

<sup>54</sup> It is also not possible to say, that the savings in the phase of recession (when we suppose limited range of investment opportunities) are than invest in the phase of expansion.

<sup>55</sup> Röpke [1936], p. 99

As we see in the chart above, the amount of investments persistently exceeds the amount of savings. These conditions are enabled by the issue of additional money instruments which support demand for capital goods and factor of productions. Excessive rise in prices of inputs and then consumer prices is the inevitable consequence of this policy. This growth in prices lowers real consumption, which is precisely the condition for creation of savings. But in this case, consumption is lowered by so-called “enforced savings” as a consequence of expansion of medium of exchange.

So events in the sphere of consumption goods are only outgrowth of the development in the sphere of capital goods. Growth in prices of production goods pushes up prices of consumption goods and, on the contrary, makes the purchasing power of consumers lower. Then slump in economic activity comes up, usually supported by growing interest rate of the central bank as a reaction to rising prices of consumption goods (and not production goods). This is the reason, why for example production price index or index of producers’ prices (industry, agriculture, services, etc.) belong among so-called „advanced indicators“.

Reisman (1996) suggests indicator of total economic activity that will fully display the business cycle (economic activity respectively) fluctuation<sup>56</sup> - „gross domestic revenue“ (GDR). This indicator can show not only expenses for consumption but also for production goods that is by the theory considered as a dominant part of economic activity. Thanks to this fact GDR really displays total economic activity. The construction of GDR is completely based on the items of national accounts<sup>57</sup>.

First we summarize total uses in the economy (TU), i.e. uses side of goods and services account. On this account, there are summarized the amounts of final consumption expenditures (FCE), intermediate consumption (IC) and export of goods and services (EX).

$$TU = FCE + IC + EX$$

When gross operating surplus (GOS) is subtracted from TU<sup>58</sup>, we obtain costs other than depreciation (d). This item represents expenses for the production purposes that are mostly away from the attentions of the GDP<sup>59</sup>.

$$d = TU - GOS$$

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<sup>56</sup> Without necessity of application supplementary indicators and displaying business cycle development as indicated monetary theory of business cycle.

<sup>57</sup> Johansson [2002]

<sup>58</sup> To exclude the double counting in the following procedure of GDR compilation.

<sup>59</sup> Some part of this costs influence the GDP as a intermediate production.

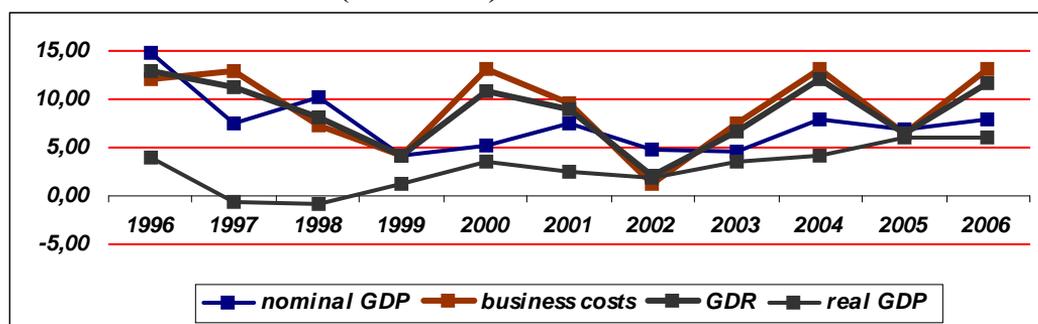
Now we can get GDR as a sum of GDP and cost other than depreciation.

$$GDR = GDP + d$$

As we can see, GDR contains consumption expenditures (final consumption, export) and production expenditure (intermediate consumption, investments). By including all of the expenditures for consumption and production purposes, this indicator has the ability to show changes in the economic activity sooner than GDP, because GDR, contrary to GDP, concentrates mainly on the process of production. The fluctuation of GDR is more volatile, because the majority of this indicator is made by production expenditures that fluctuate very strongly and are more sensitive to monetary policy.

Let us illustrate the difference between GDR and GDP in the case of the Czech Republic. Following chart compares the development of nominal and real GDP, GDR and business costs (BC)<sup>60</sup>. It is clear that fluctuations in GDR are more significant and in essence, this fluctuation is formed by fluctuation in production expenditures which is the logical consequence of dominant role of production in economic activity together with dominant role of production expenditures in the GDR indicator.

**Chart 3: Year-to-year changes in nominal and real GDP, GDR and business costs in the CR (1996-2006)**



Source: Rybacek [2008]

Such a graphic analysis of GDR is not sufficient for business cycle fluctuation analysis. Increasing money stock results in increasing amount of revenues (expenses), this coherence is in essence tautological. The crucial point here is the purpose which are additional funds used for. There are two alternatives, newly issued money can be used in exchange either for consumption or for investment goods.

<sup>60</sup> Expenditures made for the purpose of production,  $B = I + d$ , where I is investments as understand in the case of national accounts.

This different effects on different groups of prices and incomes is the crucial point of the business cycle mechanism. Because newly issued money will be received, sooner or later, by entrepreneurs (producers), it is primarily the demand for investment goods that will be encouraged. The amount of investment expenses is rising more rapidly than consumption goods. For that reason, the turning point in the business cycle lies in the sphere of production of capital goods. In other words, boom and bust aren't induced by changes in consumption but in production process creating goods, services and incomes.

In the phase of boom, share of investment expenses in GDR rises. On the contrary, the phase of bust is characterized by increasing share of consumption expenses because of unfavorable prospect of the economy and readiness to invest. Restricted investment expenses<sup>61</sup> in the phase of bust will result in decreasing exploitation of factors of production and diminishing amount of production creating incomes that are necessary for subsequent consumption. As a consequence, rising prices of consumption goods caused by strong demand and lack of capital at the end of the boom is replaced by decreasing prices at the turning point of the economic activity. Hence, again, economic turns can be seen in the production sphere of the economy.

Because the reason for the fluctuation caused by changes in monetary conditions is decreasing dynamics of investment expenses, which are in most not included in GDP, identification of the position in business cycle can be significantly different by application of GDP and GDR. The difference is convincingly showed by Johnsson<sup>62</sup>. GDR is strongly oriented on production and because consumption is necessarily preceded by production, GDR shows changes in the business cycle development of the economy sooner than GDP.

As was already mentioned, the rate of monetary emission as a consequence of the changes in interest rates will be immediately recorded in the development of the GDR, because new money will become receipts (costs) of economic subjects immediately. In other words, GDR will display the effect of the change in monetary policy on real economy with a very short delay (in comparison to the GDP). In the following chapter, we will use this features of GDR for analysis of the change in monetary condition which is called monetary integration and for the process of business cycle synchronization.

#### **4. Monetary integration and the business cycle**

Integration into monetary union implies fixation of the exchange rate. By fixing the exchange rate, common monetary policy is enforced by simultaneous

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<sup>61</sup> The investment activity is furthermore weakened by decreasing profitability, worsening availability of credits. If the excessive monetary expansion would not keep on, the profits wouldn't be encouraged and wouldn't enable producer to repay credits.

<sup>62</sup> Johnsson [2002]

existence of the free capital movement. Different setting-up of the interest rates and arbitrage capital flow would give rise to pressure on rise or drop of the (fixed) exchange rate. This fact is well known as a so-called “impossible trinity”. By the monetary integration, the economy will give up not only the exchange rate, but also independent monetary policy.

The above mentioned facts are taken to be the costs of monetary integration. Elimination of the exchange rate risk and more transparent price comparisons are supposed to be the benefits of this process. The more are the benefits advantageous, the more intensive is the economy involved in international trade because this facts lead to business cycle synchronization. As a example can serve the international linkage of Czech and German economies. To be specific, because 40 percent of Czech export is intended for German markets, the economic growth of German economy can very strongly influence the business cycle of the Czech economy

If the economies are going through a similar business cycle fluctuation, they are regarded as appropriate candidates for monetary integration. The intensity of mutual business relation is emphasized in the essay of Frankel and Rose<sup>63</sup>, that also mention increasing specialization as a consequence of the withdrawal of foreign trade restrictions. But the business cycle synchronization will be enforced despite the increasing specialization, because of intra-branch trade. Zhang and Artis<sup>64</sup> examined the effect of ERM creation on business cycle synchronization. They conclude that policy disciplines imposed by this change in the monetary condition leads to the more tightly business cycle development among European countries.

Darvas a Szápary<sup>65</sup> also examined business cycle synchronization in the enlarged European Union on the base of empirical evidence. Their research based on the GDP points out the increasing synchronization of business cycle in the case of the „core“ of monetary union and also in the case of countries on the periphery of monetary union. It is also important to mention that the least synchronized component of GDP in the analysis of Darvas and Szápary was consumption<sup>66</sup>.

Following analysis draws attention also to the eurozone and its members' business cycle synchronization. Because of difficult availability of necessary data, the analysis is not oriented on all countries of the eurozone. The analysis is based on the assumption that GDR is better tool for business cycle description than GDP. We examine the hypothesis that synchronization of the business cycle will be enforced by monetary integration in the case of economies in which cycles has not been synchronized before the monetary integration.

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<sup>63</sup> Frankel, Rose [1998]

<sup>64</sup> Zhang, Artis [1995]

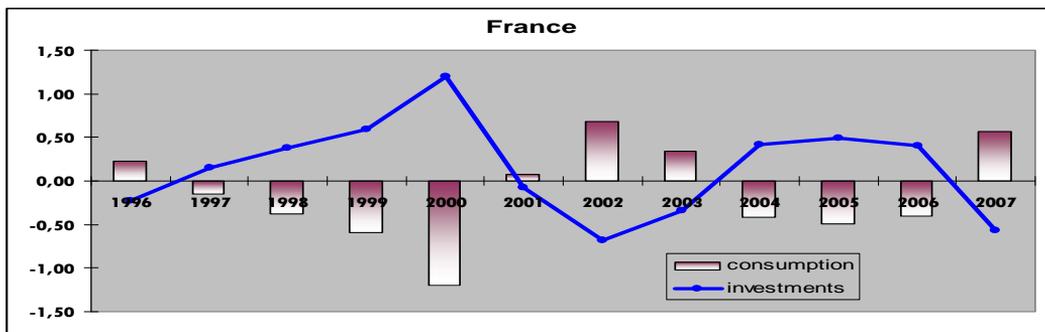
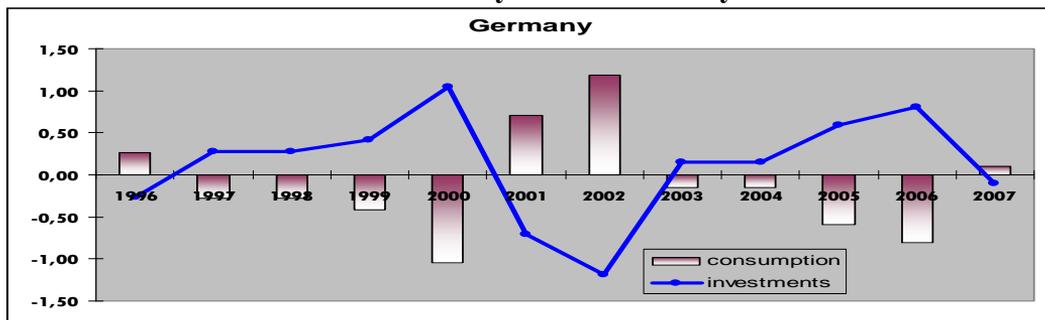
<sup>65</sup> Darvas, Szápary [2004]

<sup>66</sup> dtto. this phenomenon is also called „consumption-correlation puzzle“.

## 5. GDR and monetary integration

According to some authors<sup>67</sup>, business cycle synchronization is a self-enforced feature of the monetary integration. In other words, cycles can be synchronized by common monetary policy itself<sup>68</sup>. Is there some empirical evidence for this statement? As was mentioned above, GDP puts emphasis on consumption expenditures. But most sensitive to changes in monetary condition (as in the case of monetary integration) are investment expenditures. GDR gives us different picture of economic activity fluctuations. Let us have a look at so-called driving forces of the European integration, i.e. France and Germany.

**Chart 4 and 5: GDR of Germany and France in years 1996 - 2007**



**Source: Eurostat, own computation**

As we can see in charts 4 and 5, business cycles of these economies were fully synchronized already before the monetary integration which just goes to show the importance of mutual business relationships for business cycle synchronization. Naturally, the monetary integration did not disturb synchronized business cycle fluctuations. After monetary integration, business cycles in both of economies turned into boom with relatively strong increase in investment expenditures

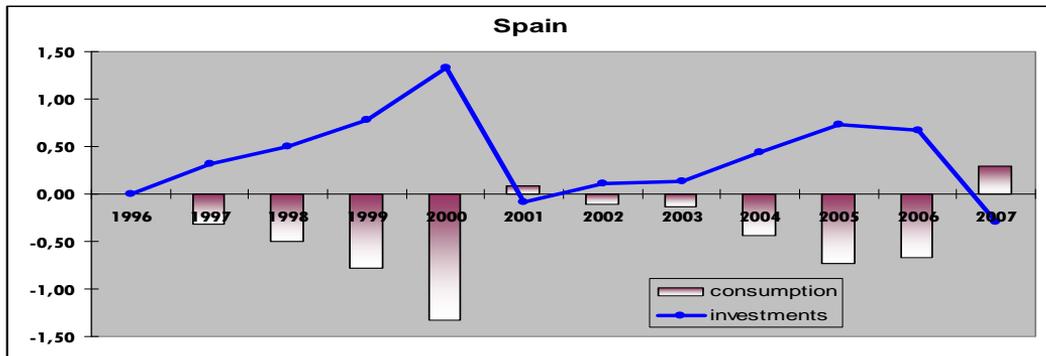
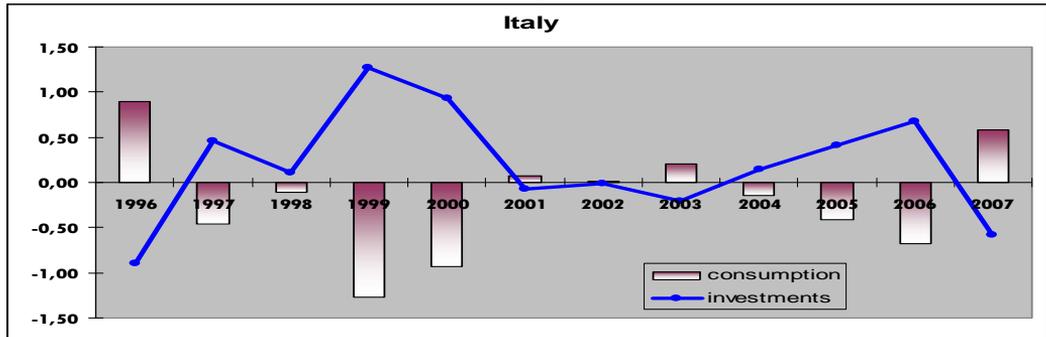
<sup>67</sup> Kwan [1998], Glavan [2004]

<sup>68</sup> Kwan [1998]

lasting till year 2006. In the year 2007 the business cycle of both of these economies turned into bust. Let us compare fluctuation in the above mentioned economies with business cycle in economies of Italy and Spain.

The business cycles of Italy and Spain were also synchronized before the monetary integration, partly each other, partly with already mentioned economies of Germany and France. We can conclude that business cycles of these economies were synchronized before as well as after the fully monetary integration.

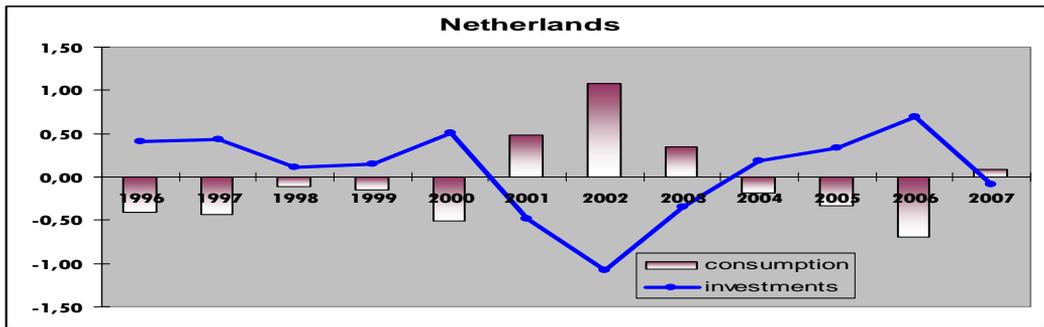
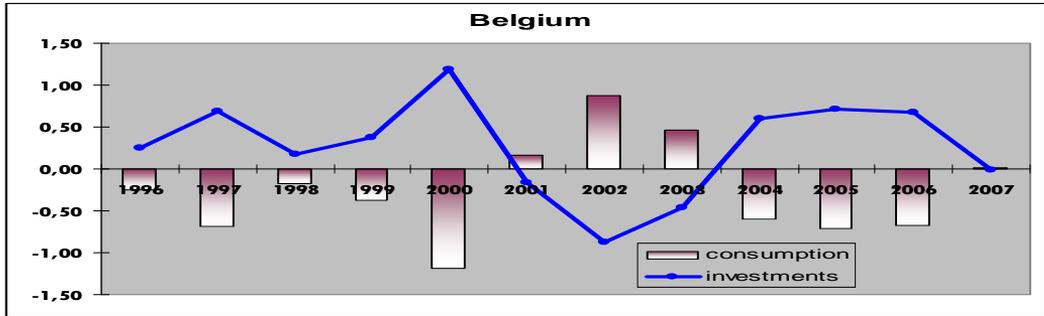
**Chart 5 and 6: GDR of Italy and Spain in year 1996 - 2007**



**Source: Eurostat, own computation**

Now we check fluctuation in economic activity in other two European countries, the Netherlands and Belgium.

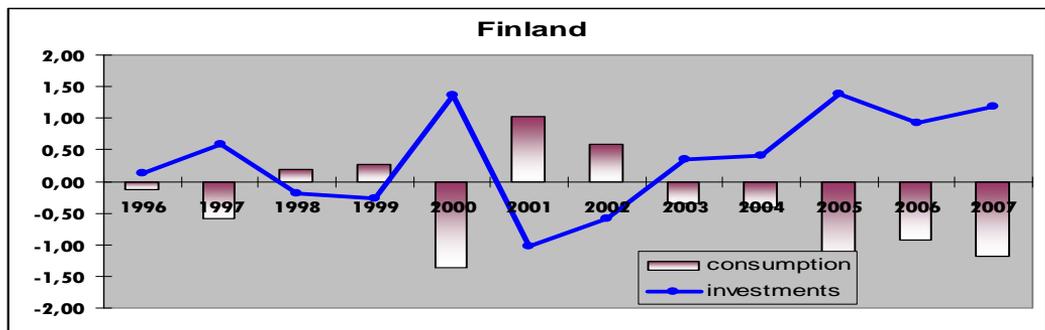
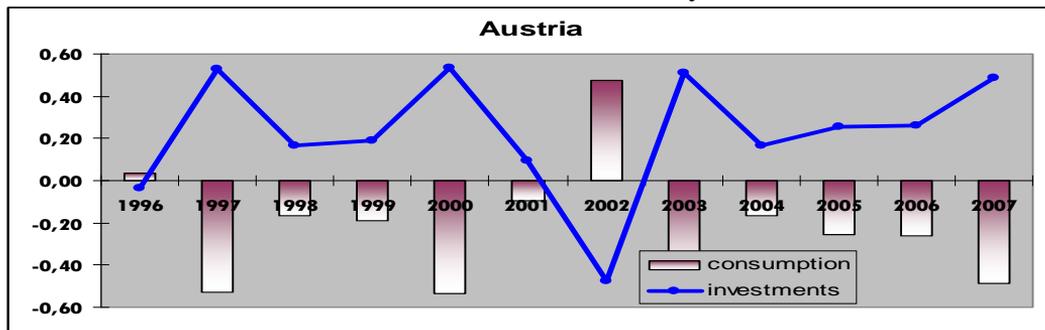
**Chart 7 and 8: GDR of Belgium and the Netherlands in years 1996 and 2006**



**Source: Eurostat, own computation**

Both economies have strong business contacts with their geographical neighbors, first of all Germany and France. Strictly speaking, business cycle of this countries is synchronized with cycles of above mentioned countries before as well as after monetary integration. Countries, which we have examined yet show almost identical business cycle fluctuation in the whole period. Now we draw our attention to other countries, Austria and Finland.

**Chart 9 a 10: GDR of Austria and Finland in years 1996 - 2006**

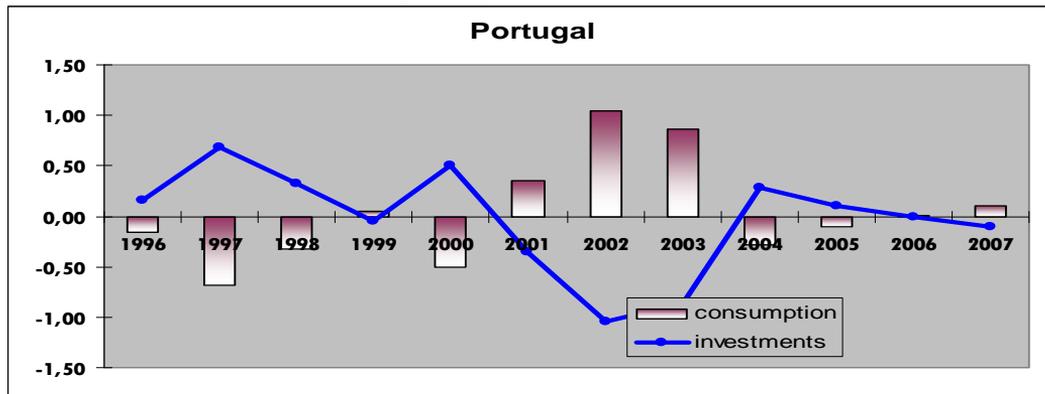


**Source: Eurostat, own computation**

Austrian economy is strongly connected to German economy, not surprisingly, Austrian business cycle is almost identical to the one in Germany. More interesting case is geographically more distant economy of Finland. The cycle of Finland is much more fluctuating between 1996 and 2002 than up to now examined countries. After the monetary integration, the business cycle synchronization got ahead, the share of investment expenditure started to increase in 2003. In the year 2007 we can see different course of the business cycles in comparison to other European countries.

Portugal is the last country with sufficiently long time series of necessary data. Business cycle in Portugal was very different from other countries which in 2003 created the monetary union. After the euro adoption, there is boom described as a growth in investment expenditures in comparison with consumption expenditures. Business cycle in the case of Portugal started to be synchronized after the monetary integration.

**Chart 11: GDR of Portugal in years 1996 - 2007**



**Source: Eurostat, own computation**

We can conclude that in the case of Portugal synchronizing influence of monetary integration has occurred. Portugal economy was in the situation of bust, even in year 2003. But then the development turns to the phase of boom lasting till year 2006.

As we have showed in our analysis, strong mutual relations make the business cycle synchronized. In the case of countries with different business cycle, monetary integration makes the business cycles synchronized (Finland, Portugal). This seems to confirm the hypothesis that monetary integration has a synchronizing effect on business cycle fluctuation, therefore, the business cycle synchronization is self-enforced feature of monetary integration.

## **5. Conclusion**

This analysis, based on the indicator GDR, shows that monetary integration seems to have an synchronizing effect on business cycle fluctuation of members economies owing to the effects of common monetary policy on investment activities. Based on this analysis we can suspect that business cycle synchronization really can be a self-enforced condition of monetary integration. In addition to that, because of general fall in investment expenses in year 2007 we can assume that current economic downturn had started in the biggest eurozone economies already more that one year before official downturn displayed in the GDP. In other words, significant changes in production process entailing in subsequent changes in consumption started already in 2007.

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ENTREPRENORIAL ACTIVITY VERSUS ENTREPRENEURSHIP  
EDUCATION

Flavia Anghel, Bogdan Glăvan\*

**Abstract:** *Entrepreneurship is one of the fastest-growing discipline throughout the world. However, the importance of entrepreneurship in economic theory is not new and consistent interest in this topic can be traced back to almost a century ago. As with any young discipline, the role and content of entrepreneurship education remains controversial. It seems difficult to decide if entrepreneurship is rather “science” than “art”, or if can be divided between teachable and non-teachable elements, or if entrepreneurship courses should focus on the advancement of personal enterprising attributes or on the ability to start, develop and manage a firm. This paper questions the relevance and appropriateness of entrepreneurship education. The results show that there is still in important gap between the prescriptions of entrepreneurship courses and training programs, on the one hand, and the insights of entrepreneurship theory, on the other hand.*

**Keywords:** entrepreneurship education, entrepreneur abilities, innovation, uncertainty, entrepreneurship theory

JEL Classification: A20, B10, L26

### Introduction

Entrepreneurship is considered an essential ingredient for strong innovation and economic growth, especially in a knowledge-based society. It is widely believed that entrepreneurial activity can be spurred through entrepreneurship education. Consequently, entrepreneurship is one of the fastest-growing disciplines throughout the world. However, the importance of entrepreneurship in economic theory is not new and consistent interest in this topic can be traced back to almost a century ago. Economists such as Joseph Schumpeter, Frank Knight and Israel Kirzner have emphasized the role of the entrepreneur in the market process of resources' allocation.

As with any young discipline, the role and content of entrepreneurship education remains controversial. It seems difficult to decide if entrepreneurship is

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rather science than art or if can be divided between teachable and non-teachable elements, or if entrepreneurship courses should focus on the advancement of personal enterprising attributes or on the ability to start, develop and manage a firm. A growing literature attempts to evaluate the effects of entrepreneurship education and so far the results are rather mixed.

This paper questions the relevance and appropriateness of entrepreneurship education. It attempts to clarify if entrepreneurship can be taught, in light of the most important theories of entrepreneurship. The results show that there is still an important gap between the prescriptions of entrepreneurship courses and training programs, on the one hand, and the insights of entrepreneurship theory, on the other hand. Therefore, a closer contact between entrepreneurship courses and economics should deliver important gains for both disciplines.

## **Entrepreneurship in economic theory**

Entrepreneurship has received much attention in the literature. In what follows, we offer a brief overview of the notion of entrepreneurship.

### *1.1. Schumpeter*

Schumpeter's (1911; 1939) well-known concept of the entrepreneur as innovator is a prime example of an idea that is much cited, but perhaps little used. Schumpeter's entrepreneur introduces "new combinations" – new products, production methods, markets, sources of supply, or industrial combinations – shaking the economy out of its previous equilibrium through a process Schumpeter termed "creative destruction".

Perhaps Kirzner best described the market impact of Schumpeter's entrepreneur when he wrote: "...for Schumpeter the essence of entrepreneurship is the ability to break away from routine, to destroy existing structures, to move the system away from the even, circular flow of equilibrium" (1973, p. 127).

### *1.2. Kirzner*

Another well-known approach in economics is Kirzner's (1973; 1979; 1992) concept of entrepreneurship as "alertness" to profit opportunities. The simplest case is that of the arbitrageur, who discovers a discrepancy in present prices that can be exploited for financial gain. In a more typical case, the entrepreneur is alert to a new product or a superior production process and steps in to fill this market gap before others. Success, in this view, comes not from following a well specified maximization problem, but from having some insight that no one else has. As in Schumpeter's vision, Kirzner's entrepreneurs do not own capital; they need only be alert to profit opportunities. Because they own no assets, they bear no uncertainty, and hence cannot earn losses; the worst that can happen to an entrepreneur is the failure to discover an existing profit opportunity. For these

reasons, the link between Kirznerian entrepreneurship and other branches of economic analysis, such as industrial organization, innovation, and the theory of the firm, is weak. Hence Kirzner's concept has not generated a large body of applications.

### *1.3. Cantillon, Knight, and Mises*

An alternative to the foregoing accounts is that entrepreneurship consists of judgmental decision-making under conditions of uncertainty. According to Cantillon's original formulation, the entrepreneur is a specialist in taking on risk. He "insures" workers by buying their products (or their labor services) for resale before consumers have indicated how much they are willing to pay for them. This idea was refined by the U.S. economist Frank Knight (1921), who distinguished between risk, which is insurable, and uncertainty, which is not. Risk relates to recurring events whose relative frequency is known from past experience, while uncertainty relates to unique events whose probability can only be subjectively estimated. Changes affecting the marketing of consumer products generally fall in the uncertainty category. Individual tastes, for example, are affected by group culture, which, in turn, depends on fashion trends that are essentially unique.

Entrepreneurs, in Mises's (1949) understanding of the market, make their production plans based on the current prices of factors of production and the anticipated future prices of consumer goods.

Judgment is distinct from boldness, innovation, alertness, and leadership. Judgment must be exercised in mundane circumstances, for ongoing operations as well as new ventures. Alertness is the ability to react to *existing* opportunities while judgment refers to the creation of *new* opportunities. Those who specialize in judgmental decision-making may be dynamic, charismatic leaders, but they need not possess these traits. In short, in this view, decision making under uncertainty is entrepreneurial, whether it involves imagination, creativity, leadership, and related factors or not.

## **Approaches to teaching entrepreneurship**

It is clear that "entrepreneurship" is a highly elastic term therefore it is not surprising that entrepreneurship curricula vary widely in content and approach. How are all these aspects of entrepreneurship taught? Let us consider each of these elements in turn.

*a. Managing existing resources.* Effective management of existing resources, whether in new or established organizations, requires not only technical business skills (accounting, marketing, finance, business law), but also leadership and strategic decision making. These subjects, of course, constitute the core of most undergraduate business programs. Such courses typically employ a

combination of traditional classroom instruction (lectures and discussion), applied team projects, and, increasingly, the case method.

*b. Acquiring new resources.* Many undergraduate entrepreneurship courses focus on the acquisition of new resources: writing business plans, acquiring venture capital, marketing new products, acquiring intellectual property, and so on. These skills are usually taught through a combination of basic analytical principles, historical case studies and examples, classroom simulations, and real-world projects.

*c. Identifying existing opportunities and creating new ones.* An increasing number of entrepreneurship courses focus not on the mechanics of running a business enterprise, but on identifying opportunities for creating new sources of value. Opportunity identification involves not only technical skills like financial analysis and market research, but also less tangible forms of creativity, team building, problem solving, and leadership. While value can of course be created not only by starting new activities, but also by improving the operation of existing activities, courses in opportunity identification tend to emphasize the launching of new ventures (firms, products, or services). But can the necessary attributes be acquired in the classroom? McGrath and MacMillan (2000) argue that particular individuals have an “entrepreneurial mindset” that enables and encourages them to find opportunities overlooked or ignored by others, and that this mindset is developed through experience, rather than formal instruction. Entrepreneurs with experience owning and operating small businesses tend to be better at identifying new opportunities than those potential entrepreneurs who lack such experience. This suggests that opportunities for teaching opportunity identification may be limited.

*d. Bearing uncertainty, exercising alertness, fostering technological or organizational innovation, and adjusting to change.* Because these are economic functions, rather than attributes of particular individuals, it is less clear how such activities can be taught through formal instruction. Mises expresses strong skepticism on this point. entrepreneurship, Mises writes, is a fundamentally creative activity: “What distinguishes the successful entrepreneur and promoter from other people is precisely the fact that he does not let himself be guided by what was and is, but arranges his affairs on the ground of his opinion about the future. He sees the past and the present as other people do; but he judges the future in a different way” (Mises, 1949, p. 585). It is clear, moreover, in Kirzner’s formulation, that “alertness” cannot be learned, that it cannot be acquired through investments in education and training or from on-the-job experience.

### **Entrepreneurship and economics: is there a trade-off?**

The foregoing remarks indicate a gulf between economists’ conceptions of entrepreneurship, as the driving force behind the market economy, and those practical manifestations of entrepreneurship studied in the classroom.

One reason economists neglected the theory of the firm is that they thought the internal workings of the business firm were beyond the scope of economic analysis. In Pigou's (1921, p. 463) words: "It is not the business of economists to teach woolen manufacturers to make and sell wool, or brewers how to make and sell beer, or any other business men how to do their job. If that was what we were out for, we should, I imagine, immediately quit our desks and get somebody – doubtless at a heavy premium, for we should be thoroughly inefficient – to take us into his woolen mill or his brewery".

Likewise, the technical arts of managing existing resources, acquiring new resources, identifying and creating opportunities, bearing uncertainty, and innovating—the subjects of most entrepreneurship courses – are perhaps regarded as outside the economist's legitimate expertise.

Or, as Harvard Business School professor Howard Stevenson puts it, "if people have innate musical talent, you can't necessarily teach them to become Beethoven. But if they have that innate talent, then they probably would still benefit from piano lessons" (Stevenson et al., 2002).

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**SPECIFIC EVOLUTIONS IN THE MANAGEMENT OF  
CONSTRUCTION BUSINESSES**

Iulian Patriche\*

**Abstract**

*The business market in the domain of constructions takes into account the system of specific relations generated by the activities developed by the enterprises which offer their products and services realised in the respective domain to other enterprises or organisations and to the population. As a result, the system of business relations is particularised, within the framework of a global market, by the nature of the products and by the clients' characteristics who are interested in the respective products and services, which individualizes the market of goods and services in the domain of constructions through the manner of manifestation and materialization of the offer and demand and through the way in which transactions are realised. Consequently, in order to delimit the constructions' market and especially to analyse managerial evolutions of businesses in the respective field, it is necessary to take into account a set of specific elements. In this sense, we take into account: the new coordinates of evolution in the constructions' sector, the consumption, number, category and importance of the firms which represent possible clients; the type of problems which form its offer of merchandise; the system of payment.*

Keywords: business management, business market, transactions.

JEL Classification: M20, L60, L74

The evolution of contemporary society realizes the fact that the domain of constructions has become one of the most complex fields of activity of the economy. Finding a solution to the problems regarding durable development, providing the economy with the necessary infrastructure, ensuring houses for the population, protecting the natural environment, etc., all these aspects preoccupy specialists, politicians and representatives of civil society. Another piece of the puzzle is establishing a balance between rational functionalism and individualism. However, the most complex problem is the excessive crowding in some areas, especially in big cities, with all its consequences – major difficulties in traffic, the reduction of natural environment, the lack of houses and space, excessive pollution, etc. The modern man must always try to solve such priorities through a rational and efficient development of the activities in the constructions field.

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Moreover, in the context of a double transition towards a society based on knowledge and durable development, new paradigms of production and consumption appear. It is necessary to switch the approach, from one based on resources to one based on knowledge, from one based on mass problems to one based on new concepts, durable products and services<sup>69</sup>. In such a context, activities in the constructions field will have to be revised and based on research and reoriented through an adequate business management, suitable for each market area.

### **A business management based on the exigencies of durable development**

■ The first aspect that we want to point out through this analysis refers to the necessity of shaping and promoting through research – technological, ecological, of eco efficiency, economic, sociologic and political – a business management oriented towards the value of the specific elements of the contemporary style in urban constructions, protecting the environment, revising the construction of the urban circulation system and the location of satellite towns.

• As far as the value of specific elements of the constructions' contemporary style is concerned, we point out the managerial preoccupations, on an international level, to study and generalize the possibilities of promoting an offer – depending on the conditions and characteristics of each market area – based on the construction of administrative or business buildings, with many floors – over 30-40 floors, in order to save basic space; with a structure of metallic resistance, constructed rapidly and combined with large glass front side pieces. The management of such business practices should consist of a functional promotion of adequate and high quality materials, industrialization and simplification of prefabrication processes extended to most of the building so that the beneficiaries are provided with the necessary buildings, flexible but resistant at the same time. Moreover, the local particularities have to be taken into account – tradition, climate, sources for materials and the possibilities for reflecting the environment – in order to have a modern but also natural background in the middle of the beneficiary city<sup>70</sup>.

• Protecting the environment, good economic activities and the security of the citizen impose special managerial measures in the actual realization of the project. In the modern world, building sites differ from those from the past – in towns, the field around the constructions has to be clear and measures have to be taken in order protect the passers-by, loading materials should be made rapidly, organised and with special equipment. The process of production should develop

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<sup>69</sup> \*\*\* Euroabstracts (publicată de Comisia Europeană), Luxemburg, Octombrie, Vol. 40, Nr. 5/2002, P. 13.

<sup>70</sup> I. Patriche, Piața construcțiilor în România, Ed. Uranus, București, 2003

quietly, in a clean manner, without dust and mud and the obligations imposed by authorities should be respected by all those involved.

- Revising the way of construction and establishing a system of urban circulation determined the necessity of elaborating research and resulted in a series of mandatory exigencies which should be put in practice by constructors. Managers of construction businesses should try to ensure rapid working, to offer street directions so that vehicles circulate independently from passers-by on big streets or to promote systems of superposed circulation.

- One of the specific preoccupations of business management in the domain of constructions in the present stage of evolution of modern society is represented by the exigencies caused by the emergence of satellite towns. In this sense, in order to reduce the concentration of population in the centre of the city, some metropolises adopt policies of establishing satellite towns, maintaining an adequate social framework for the modern man. The offer which represents the core of the business is characterised by the fact that renouncing in many situations at the principle which separates the collective houses from the individual ones, a large variety is obtained in the physiognomy of such satellite-cities<sup>71</sup>. The idea is that individuality and the proximity of nature are points of reference, taking into account the fact that only a part of human demands can be satisfied within the walls of a house. Outside there have to be areas destined to social, educational and cultural activities, commercial networks, green spaces, etc. The offerers should take into account the fact that the modern citizen is entitled to a large variety of possibilities in an unproductive atmosphere and a safe environment. Also, in order to realize such projects, specialists from different and numerous socio-economic fields should be consulted.

### **Promoting a vision of perspective in construction businesses**

- Promoting a vision of perspective in the management of businesses in the domain of constructions represents another side of the specificity of the respective domain. In this sense, we take into account the implications of the global durable development, the impact of the generalization of exigencies in the informational society on the construction activity, the occupation of the subterranean space, the new tendencies in establishing the European system of transportation and the contribution of the constructions domain in the development of a knowledge-based society.

- The implications of the global durable development in the domain of constructions represent complex aspects; this sector suffers the impact of the complexity of the value change among nations and of the amplification of new concepts regarding the globalization of contemporary economy and the

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<sup>71</sup> L. Abdelmalki, P. Mundeler: *Economie de l'environnement*, Ed. Hachette, Paris, 1997

development globalization. Indeed, the domain of constructions – through its proportions and system of realization – even if it is strongly affected by the real estate crisis – it has become in contemporary world an extended sector, characterised by diversity and dynamism. If at the beginning of the century the enterprises which operated on different local markets tried hard to surpass their limits in order to reach a regional market and, finally, a national market, in the past decades the orientation of the constructions offer and services, the standardisation of products, the development and implementation of national and international banking networks and the modernization of communication means have lead to major changes in the business approaches, including in constructions, given the fact that the exchanges among countries have intensified and that national markets tend to be a part of a large international market, thus emphasizing the necessity of a revision of the managerial problems in a globalised world, in simple, polycentric terms<sup>72</sup>. Concerning the evolution of this phenomenon, we consider that it is necessary to point out a special aspect regarding the impact of the respective phenomenon on the business management in the constructions domain. In this sense, we take into account the idea according to which the phenomenon of globalisation is not conceptually based on notions or adequate theses or on a system of statistic indicators, able to capture direct and indirect connections which take place between economic agents in different states and the local authorities, and regarding the multiple relations among states and continental integration organisms or with international vocations, globalisation exists and represents a real and omnipresent phenomenon in all areas and domains<sup>73</sup>. Moreover, the more dynamic, concentrated and unpredictable the economic life becomes, the more important are the capacities of reaction, intelligence multiplication and of realisation of the efforts' synergy, being amplified in this way the need to introduce a so-called network in the pyramid systems of leadership, on a micro and macro economic level and especially on an international level<sup>74</sup>. The respective concept takes into account an integrated system of communication among the interconnected elements and other multiple dimensions representing an adequate answer to the necessities of rapid adaptation. Through its content, the respective concept gives an answer to the process of globalization which, through connections among the enterprises from different countries, free circulation of goods and services, money and people, produces not only unpredictable structural changes, but also multiple interdependences and feed-back relations, generating new game rules in interstate relations and imposing a new modus operandi for all economic agents – operators on the market – worldwide, in order to ensure a certain continuity between the micro, macro and international economic levels.

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<sup>72</sup> M. D. Popescu, *Globalizarea și dezvoltarea trivalentă*, Ed. Expert, București, 1995

<sup>73</sup> I. Patriche, *Canale de distribuție și logistică*, Ed. Uranus, București, 2007

<sup>74</sup> H. Azonlay, *L'entreprise en réseaux. Le réseau commercial*. Editaz, 1995

In such a context, construction business managers have to take into account, in order to maintain a good orientation, several specific aspects of major importance which have begun to assume shape on the construction market.

~ So, in many developed countries, since the end of the past century, the population's tendency to leave the centre of the city in order to build individual houses beyond the town limits is getting stronger and stronger, as a consequence of work decentralization caused by the emergence of other kinds of activities related to informatics<sup>75</sup>.

~ Moreover, a progressive reduction of family dimensions and the increase of exigencies regarding the level of comfort – available space – take place and also a certain decrease of the purchase power of the population which determines a quantitative reduction of the built space at the same time with the necessity of an enhancement of the construction quality as a result of the increase of potential beneficiaries' exigencies – fewer but more demanding.

~ Another tendency assumes shame, namely the tendency that the population's preferences are oriented towards large individual houses, functionally spaced, surrounded by green space, with special equipment – garages, pools, small annexes for complementary activities, such as: work shops, greenhouses, etc.

~ New collective needs appear constantly regarding the enhancement of the life standard. It refers to the increase of exigencies concerning the coordinates of collective comfort – spaces, equipment, dimensions, etc.; the increase of demands for new kinds of special equipment – educational, cultural, commercial, health care, etc.; new exigencies regarding modern and rapid transportation, especially in urban areas.

- Exploiting the subterranean space – a modern tendency in the orientation of businesses in the domain of constructions – represents another challenge for managers. As specific elements, issues concerning the reconsideration of the offer often appear both regarding the proper constructions and the construction services. Such a rethinking of the ways in which the offer is established should be based on the idea according to which the present world wide tendencies are manifested through the development of subterranean structures in order to have more space on the surface<sup>76</sup>. The maze of streets on the surface will correspond to a similar one in the subterranean, together with commercial networks, parking lots, warehouses, restaurants, etc.<sup>77</sup>

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<sup>75</sup> \*\*\* Construction Beyond 2000. Future of construction. Construction of the Future Pre Proceedings, Espoo – Finlanda, 1992

<sup>76</sup> Ph. Kotler, H. D. Haider, I. Rein, Marketingul locurilor, Ed. Teora, București, 2001

<sup>77</sup> M. Dessolain: L'avenir appartient aux "Centre de vie". În revista Libre – Science Actualités, Nr. 1637, 1999

- Important specific aspects – in business management in the domain of constructions – gradually assume shape through the new tendencies regarding the establishment of a European system of transportation. In this sense, we take into account, especially, two aspects: the rehabilitation of the infrastructure in big cities and the construction of a European system of transportation.

~ The first aspect is represented by the main tendencies regarding the rehabilitation of the infrastructure in big cities and refers to the construction of new transportation systems – intelligent streets – subterranean transportation combined with transportation of high speed on the surface, etc.

~ The other aspect assumes shape starting from the idea according to which there is a strong connection between the existence of a good system of transportation and economic prosperity. As a result, the need to extend and enhance the European communication network appeared, especially in the East and centre. In the context of such preoccupations, a new managerial approach emerged, a unitary approach, which would ensure the development of an integrated vision of all the infrastructure's components – streets, railways, airports, etc.

- The business world in the constructions domain is also characterised by strong contradictions between what is being realised and what is already realised – more or less well constructed from the point of view of the architecture, location, integration in the available space, public utility, etc. As a result, in the business management from the respective sector, important specific aspects generated by the rehabilitation of the built space have emerged, aspects which will shape the respective rehabilitation as a perspective tendency of major importance and as a novelty in the field. We take into account the fact that a progressive reorientation emerged nowadays in the constructions domain in some occidental states, from the construction of new buildings to the rehabilitation of the space already built. Such an idea and a certain discontent of the population regarding the unsuccessful construction of certain buildings overlap, construction which did not bring an enhancement and the transformation of the environment lead to the loss of the respective area's identity. In this sense, the basis of new businesses should be oriented so that the rehabilitation of an already built area is made in a manner that ensures an economic change for the better and corresponds to the socio-cultural requests of the inhabitants in that area<sup>78</sup>. In order to succeed in such actions, managers in the constructions domain should think of measures which refer to the determination of the typological character of the buildings in the rehabilitated area and the establishment of a model, the utilization of allowed materials and even the formulation of new recommendations regarding the ways in which are used the rehabilitated constructions.

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<sup>78</sup> E. I. Emandi, *Habitatul urban și spațiul*, Ed. Glasul Bucovinei, Iași, 1996

- Promoting a vision of perspective in the domain of construction business management presupposes preoccupations concerning the contribution of the respective domain in the development of a human society based on knowledge. We emphasize in this sense the idea according to which the interest increase in a durable development should determine in constructions the implementation of specific measures and actions such as: the reduction and even the elimination of certain polluting methods which consume a lot of energy; the utilization of regenerative resources; avoiding materials which cannot be used after demolition; the ecologic balance through design, production, use and inhabitancy<sup>79</sup>. Of course, in such a managerial conception of businesses with such restrictions, the costs generated by the respective informational measures – ecologically, they will have to be taken into account for the preliminary determination of the realised products' price – constructions and construction services. We think that only what is necessary, simple and human should be built, with warm materials, a lot of light and colour, so that humans are stimulated to think about next generations and protecting the environment<sup>80</sup> and that the switch to an informational society should be marked in the domain of constructions also by the major transformations<sup>81</sup> in knowledge and global durable development.

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<sup>79</sup> Ph. Latour *Géomarketing*. Les Editions d'Organisation, Paris, 2000

<sup>80</sup> V. Rajanschi, Fl. Bran, Fl. Grigore, *Elemente de economia și managementul mediului*, Ed. Economică, București, 2004

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LEASING INDUSTRY IN THE ISLAMIC WORLD – CHALLENGES  
AND OPPORTUNITIES

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Abstract

*The leasing it's a form of financing through rent by the specialized financial companies in this operations, of some machines, equipments and some companies goods of the motivation to resort at this form of trade it's in the specific of some operations that they achieve or in the fact that they don't have sufficient founds of they own and borrowed to buy them.*

*Having in view the multitude of ways to buy or to get only the utilization right of an asset (the leasing, the acquisition with cash from one's own founds, the acquisition through a loan, the acquisition with the payment in rate) the beneficiary has to do a deep analyze of this sources. During this analyze, the most important factor has to be taken in consideration, it's the cost of each way.*

Keywords: Islamic Leasing, Leasing industry, Islamic Finance

JEL Classification: G21, G30, F30

The leasing it's a form of financing through rent by the specialized financial companies in this operations, of some machines, equipments and some companies goods of the motivation to resort at this form of trade it's in the specific of some operations that they achieve or in the fact that they don't have sufficient founds of they own and borrowed to buy them.

The leasing represents a private financing way that can be analyzed like a loan and the cost of this financing source can be evaluated under the form of a financial rate. It's applied the present equality values of the equivalent financing sum principle (the acquisition and the assembly cost of the loaned equipment = **E**) and the treasure outputs for the future payments for the annual rent (**CH**) and the residual value (**VR**). At equality, in present day, of the two treasure flows (equivalent input and effective output) it's been calculated the actuarial cost of the leasing as a internal efficiency rate (**KI**).

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The leasing cost brings in a natural way and the fiscal effects of this financing. The rent is a deductible expense from the profit tax payment. The part about the repayment of the loaned equipment doesn't constitute a fiscal economy for the leasing beneficiary, but for the leasing purveyor, in consequence, the leasing beneficiary is not the owner of the loaned good and it's recording an opportunity cost, determinate by the loss of the tax economy for the repayment (**A**) of the loaned equipment.

$$E = \sum_{t=1}^n \frac{(1-\tau) * CH_t + \tau * A}{(1+K_1)^t} + \frac{VR}{(1+K_1)^m}$$

$\tau$  = the profit tax rate

$t = 1, \dots, n$  years of availability of the leasing contract

$m = n + 1$

In this conditions, the leasing costs (**KI**) it's the solution for the upstairs equation that is been calculated after the methodology of the internal efficiency rate. The leasing cost for the beneficiary (**lodger**) it's the efficiency rate for the purveyor.

The decision to choose for the leasing, in report with a banking or bond loan, it's fundamental on the net present value (**VAN**), calculated after the relation:

$$VAN = \sum_{t=1}^n \frac{CF_t}{(1+r)^t} - \frac{VR}{(1+r)^m}$$

Since it's not payable the acquisition cost of the loaned good, in the **VAN** formula it's not included the diminution of the investment value (**I**). There for, the cash flows (**CF<sub>t</sub>**) will be determined in accordance with the future profits and the paid rent (the rent it's a deductive expense from the profit payment). The residual value (**VR**) it's paid in the  $m$  year, before the end of the life circle (**n**) of the loaned good. The present value it's compared with the loan one, for analyzing witch of this financing sources it's more advantageous.

The selection of financing sources of investments it's very complex as, besides the main criteria about the capital secured cost, acts a series of restrictions for the access at the capital market, the financial situation of the company, the motivation of the leading personnel of the company. If we refer to the last condition, if the employer of the company has all the assets, then he owns the business and he is responsible for all the decisions, good or bad. In this conditions, he will not approve the capital increase through the sale of new assets to the public. If it doesn't have the possibility to buy himself, then he will prefer other financing sources.

There for, the access to the bond loans doesn't have than a low number of companies, respectively the ones that offer a sufficient guarantee for thus pledges in presence of the public, in plus, the bond loan it's very complicated from the formality's point of view.

Most of the companies are not in the stock market and they don't have the possibility to negotiate the titles through the stock market. So, it doesn't have any other way but the auto financing the usual banking loan, the leasing or the assets sale.

"What is this "Islamic" leasing and how is it any different than what we are doing now?" The fact is that Islamic leasing, and what I will call, for want of better terminology "conventional" leasing, are very nearly the same. In fact, there are many more similarities between the two than differences. From a practical standpoint, there are really only three distinctive differences between the Islamic and the conventional lease:

1. *In the Islamic lease, interest related characteristics are removed. That means things like late fees, interim rents, and interest accumulation on money deposits are eliminated from the contract. It does not mean elimination of "profit". Profit is an integral part of almost all Islamic financial transactions.*

2. *There are some restrictions on the assets and/or on asset use. Islamic principles typically would prohibit involvement in areas involving such things as alcohol, tobacco, conventional finance, or pork products. The lease of assets used in connection with these industries/items would be prohibited.*

3. *The Islamic lease calls for the lessor to take real responsibilities in the ownership of the Asset. This becomes, in fact, the main difference. The conventional lease tries to contractually move the lessor as far away from asset responsibilities as possible. The Islamic lease insists that the lessor assume certain basic responsibilities as the owner of the asset.*

These three differences are minor, but important distinctions in the contractual arrangement between lessor and lessee. However, the ultimate documentation package leaves the Islamic lessor and the conventional lessor on relatively equal footing from a practical and economic standpoint.

An example of this is an Islamically designed leasing Fund that ILIC is involved in. This Fund is one of a series, and the other Funds in the series are all conventional. Because of exposure limits, these funds often join together in the financing of a single transaction. However, rather than confuse the lessee with different documentation, the Islamic documents are routinely used for ALL the funds. This is a practical and economic recognition of the equality between the conventional and the Islamic lease.

The International Leasing & Investment Co (ILIC) was organized in mid 1999 as the first large ticket, general asset Islamic leasing company in the world. While its business focus is in the Islamic countries, specifically the member countries of the Islamic Development Bank, its range of business activity is worldwide, stretching from Indonesia in the East to the United States in the West. Originally capitalized with US \$50 million, ILIC effectively controls assets of nearly half a billion dollars.

One of the mandates of ILIC as a company, is to develop the practice and use of Islamic leasing worldwide. This mandate is manifested in the Company's aggressive development of new leasing companies throughout the world. Because of this activity, ILIC is in a unique position to see and assess the potential for Islamic leasing.

So now you may ask yourself another question: "If the Islamic and conventional lease are so similar, why can't I just go ahead and used my conventional leases—what difference does it make?" The answer to that questions lies within the fundamentals of Islam. Simply stated, a contractual arrangement that does not include these differences is not acceptable under Islamic principles, and is therefore "haram", or prohibited to the Muslim practitioner. Small as they may seem, they are critical differences.

To the practicing Muslim, the principles of Islam are more than just a guide, but are rather a divine dictate that must be followed. To the Muslim, these principles outline a course of living that lead to happiness, a harmonious community, and a thriving economy. The principles must be followed with exactness, however, and thus the practicing Muslim will preferentially use Islamic finance whenever it is available.

### **Islamic lease versatility**

The Islamic lease is the most versatile of the Islamic financial products, and this makes the Islamic lease the instrument of choice for many financial transactions. This versatility within the realm of Islamic finance finds the lease used in many instances that would commonly find a different type of instrument were the same transaction done conventionally. This means that within Islamic finance, the lease will be used for a higher percentage of the overall transactions, than would be found in the conventional world.

The source of this versatility is found in two areas:

- ☞ *the rules that govern Islamic financial transactions, and;*
- ☞ *in the basic nature of the lease.*

One of the basic principles of Islamic finance is that money is not to be treated as an "asset" or "commodity". Money is looked at simply as a medium of exchange, and not as object in and of itself. Thus, In Islamic financial, an asset, other than money, must be at the base of the transaction. This asset may be bought and sold and debt generated as a result of such activity. But the money itself may not. Since it is NOT viewed as a commodity, money, including money (debt) obligations, is not able to be sold once they are originated. This means that in most Islamic financial transactions, once the underlying asset is sold, the seller and holder of any debt generated by the sale may not re-sell the obligation. It must be held through maturity by the original holder of the debt.

In conventional finance, re-sale of debt is a common practice, and constitutes the basis for conventional secondary market activity. Such activity is not allowed under Islamic financial rules.

The Islamic lease, however, provides a different opportunity. In the lease transaction, the money obligation is tied to the asset and to its use. The financier, as Lessor, retains ownership of the asset during the term of the lease, and this ownership interest, together with the obligation to pay lease payments on the use of the asset, MAY be transferred, in whole or in part at any time during the lease. This effectively provides the only viable secondary market vehicle available to Islamic finance. This also provides a huge incentive for Islamic financial institutions to use the lease as the structure of choice in Islamic financial transactions.

A second incentive for use of the lease over other Islamic financial instruments rests with the nature of the lease transactions itself. In most Islamic transactions, an asset is sold and ownership is transferred. When this transfer takes place, the money obligation becomes set (remember, there is no interest in an Islamic transactions, so interest characteristics are not present in the structure of the transaction). The conventional characteristics associated with interest, such as the potential for a variable rate and late payment interest, are not allowed. Once again, we see the versatility of the Islamic lease come to the front. Since the lease effectively runs from period to period, allowance may be made to adjust the lease payment prior to the beginning of each such period. This adjustment may be legitimately formulated to work very similar to the conventional adjustable rate.

To these special issues of versatility is added the natural flexibility of the lease transaction, and when taken as a whole, provide the practitioners of Islamic finance strong incentive to use the lease as the instrument of choice whenever possible.

From a real world situation, the practices of Islamic finance are in a resurgence. Much of the Muslim world is currently served through conventional financial institutions. However, the growth and development of Islamic financial institutions and products has led to a quickly increasing Islamic financial marketplace, and those who hope to compete in this marketplace in the future will have to provide products and services that are compatible with Islamic principles.

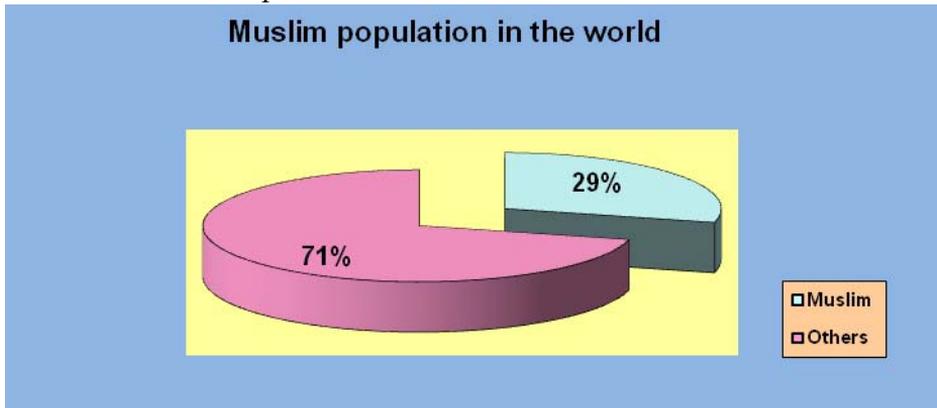
“Well,” you may ask, “Why do I need to worry about this at all?” The answer to this question lays in the demographics of the world population figures. Let’s take a look at those numbers, first from an overview standpoint.

There are approximately 6.5 billion people in the world. Depending on whose estimate you use, up to 29% of those people are Muslim. That means that over 1.6 billion people one quarter of the world’s population adhere to the principles of Islam. As a general rule, if these people are given a choice, they would have the preference to use Islamic financial products, including Islamic leasing, over conventional methods of finance. Thus, with an offering of Islamic leasing, one-

quarter of the world becomes a market with preferential inclinations towards the way you are doing business.

Regionally, these numbers obviously change, with certain parts of the world having much heavier concentrations than others. However, even in markets like the United Kingdom (2.7% Muslim) and the United States (3.75% Muslim), the total Muslim population still provides a tidy market share potential to draw from.

For example in the US marketplace, 3.75% of the leasing market represents over US \$7.5 billion in potential business. In the UK market, that 2.7% represents over US \$500 million in potential market share.



UN statistic's 2007

Using the statistical information from the Euromoney World Leasing Yearbook 2004, and combining this with the demographic estimates of Muslim population, a sampling of market potential looks something like this:

<b>Market Potential of Islamic Finance</b>			
<b>Country</b>	<b>Lease Volume (US \$ Bln)</b>	<b>Muslims as a Percentage of Total Population</b>	<b>Representative Lease Volume (US \$ Bln)</b>
<b>US</b>	204.00	3.75%	<b>7.65</b>
<b>France</b>	22.23	10.00%	<b>2.22</b>
<b>Germany</b>	39.77	3.70%	<b>1.47</b>
<b>Morocco</b>	0.54	99.00%	<b>0.53</b>
<b>Turkey</b>	1.32	99.80%	<b>1.31</b>
<b>Italy</b>	22.35	2.40%	<b>0.53</b>
<b>United Kingdom</b>	19.07	2.70%	<b>0.51</b>
<b>Russia</b>	2.00	19.00%	<b>0.38</b>
<b>Pakistan</b>	0.37	97.00%	<b>0.35</b>
<b>Nigeria</b>	0.37	70.00%	<b>0.25</b>
<b>Netherlands</b>	4.66	5.40%	<b>0.25</b>

<b>Saudi Arabia</b>	0.22	100.00%	<b>0.22</b>
<b>Canada</b>	10.44	2.00%	<b>0.20</b>
<b>Switzerland</b>	6.11	3.10%	<b>0.18</b>
<b>Sweden</b>	5.88	3.10%	<b>0.18</b>
<b>Malaysia</b>	0.28	59.00%	<b>0.16</b>
<b>India</b>	1.00	14.00%	<b>0.14</b>
<b>Bangladesh</b>	0.14	88.30%	<b>0.12</b>
<b>Spain</b>	9.30	1.20%	<b>0.11</b>
<b>Belgium</b>	<b>2.89</b>	<b>3.60%</b>	<b>0.10</b>

\* Euromoney World Leasing Yearbook 2004

Certainly, this is an acknowledged simplification of the marketplace. It is, however, also a limited view of the real marketplace and opportunity that exists. Because many of the countries that have heavy Muslim populations are also developing countries, with uncertain reporting methods available for the various economic activities that occur, much of the leasing activity that happens in these countries goes unreported.

It is important to note, however, that the market potential exists not only in the countries with predominately Muslim populations, but also in those areas where the Muslim population represents a relatively small portion of the total population. Revisiting the United States market gives a prime example of this, where, as pointed out, the representative lease volume for a relatively small percentage of the population still equals over \$7.5 billion in potential business! And remember, this is the “extra” edge that would be available to an Islamic leasing company.

Such a company does not do business just with Muslims, but is able to compete against other leasing companies in the general leasing market, whether Islamic or conventional, for all leasing business that is available.

### **Business expansion**

Islamic leasing also offers an opportunity for a leasing company to dynamically expand their business opportunities. In most of the developed countries, the market share of leasing versus other modes of financing is relatively stable. For example, in the United States market, approximately 1/3 of all capital equipment acquisitions have been made through the use of leasing. This statistic has remained relatively constant for the 25 years that I have been involved in the leasing industry.

So what happens if you want to expand your business? To have dynamic growth? You have, in fact, only a limited number of options:

☞ *You can increase the share that leasing commands in the over-all capital asset markets.* This, obviously, is very difficult to do in a mature market—

as shown by the fact that no one in the US seems to have been able to accomplish it—at least over the last 25 years. This may be a very realistic approach in a developing economy. Remember, though, that many of these developing markets have heavy Muslim populations that will demand the use of Islamic financial products.

☞ *You can take market share away from someone else.* This is the more typical way that growth occurs for an individual company. It is also the most “dangerous” for a leasing company. Typically, this approach requires tactics designed to lure existing customers away from whomever they are currently doing business. These tactics often incorporate things like easier credit standards, lower rates, etc., each of which may potentially have negative effect on the leasing company’s portfolio and business viability. Targeting a “preferential” group of the economy, such as the Muslim population, may allow a company to dynamically gain additional market share simply by offering a compatible product, and not by resorting to portfolio threatening tactics.

☞ *You can wait for the economy to grow.* A growing economy offers limited growth potential for the leasing industry. Assuming that market penetrations remains somewhat constant, the total volume of leasing business should expand with the general growth of the economy. However, this phenomena rarely, if ever, produces the opportunity for dynamic growth, and the leasing company that looks to expand its share of business through only this means will have a long and frustrating wait.

☞ *You can expand into new and/or less developed markets.* For the leasing company that is not afraid of the international environment, this may be the most attractive alternative to dynamic company expansion. Developing markets offer huge opportunity, and growth potentially can be quickly realized. Once again, however, many of the most attractive opportunities for such expansion occur in countries dominated by Muslim populations.

### **Islamic capital**

Companies operating in the realm of Islamic leasing also have an additional advantage, and that is the ability to tap into the Islamic capital markets. An estimated US \$380 billion in underutilized capital exists in this marketplace, and this capital is looking for a worthy “home” in Islamically compatible investments. And, since many of the oil producing countries of the world are Islamic, this capital base, fuelled by the booming oil economy, continues to grow.

### **Islamic finance**

Entering into the arena of Islamic leasing should be approached like any other new venture or modification of business focus. Such changes, to be successful, typically require a firm management commitment and a dedicated effort of company resources.

To make such a transition, you must have a thorough understand of exactly what you are trying to accomplish, and how Islamic leasing can help you accomplish it. You must also be willing to make the commitments required for such a change, and then be willing to take the necessary steps to qualify as an Islamic lessor. The changes required demand a clear understanding of Islamic finance and the underlying governing principles. These changes involve, among other things, changes in documentation, staff training, and a modification to business practices.

Getting expert advice early in such a transition is essential. In entering new markets, it may be prudent to partner with an existing Islamic financial institution or leasing company and/or to obtain expert consulting advice.

In this regard, Islamic financial institutions, including Islamic leasing companies, typically work with a "Shariah Committee". The Shariah Committee is a group of Islamic scholars who provide guidance to the company's business activities and practices. The Shariah Committee will review and give input into standard documentation, products, and, as necessary, individual transaction structure and other business activity, to ensure compliance with Islamic principles. Affiliating with a Shariah Committee will be a necessary step in a transition or expansion to Islamic leasing.



For those companies who are not willing and/or able to make the commitments necessary to present Islamic leasing on their own, another avenue may also be available. Coordination with an existing Islamic lessor, through a brokerage arrangement or some other relationship, may allow the company to reap fee income from Islamic transactions.

It is important, in these relationships, to bringing the Islamic lessor into a transaction early.

This will ensure that the deal is properly structured to meet Islamic rules, and will preserve the needs and desires of the client for an Islamic transaction.

There are compelling reasons for a financial services company to become involved in Islamic leasing. As the most versatile of the Islamic financial products, the Islamic lease is assuming an ever-increasing role in the arena of Islamic and world finance. The world demographics add to this compulsion by demonstrating that one-quarter of the world's population can be assumed to have a preference towards the use of Islamic financial products. Companies that wish to enhance and dynamically expand their business scope, would do well to consider the vast potential of the Islamic leasing marketplace.

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**AUTOMOTIVE INDUSTRY CRASHES INTO THE FINANCIAL  
CRISIS' WALL**

Vlad Cârstea\*

**Abstract**

*The financial crisis that affected the entire world economy through every one of its compartments did not avoid the automotive industry. As such all car manufacturers try to reduce their losses in order to resist better on a reducing and highly competitive market.*

*Keywords: financial crisis, sales figures reduction, losses, first registration tax*

*JEL Classification: L10, L62, L91*

The financial crisis that started in the US is now present in all the world economies. This state of fact was easy to foresee, because the globalization process is so advanced and the national economies tend to become a global one.

The crisis' effects were felt in all economy sectors, especially in the automotive sector, due to the fact that the car industry acts like a barometer for the wealth of the national economy.

In the United States giant car manufacturers General Motors and Chrysler, are on the edge of bankruptcy and they depended on a bailout plan that was supposed to come from the US Congress. Unfortunately, the 14 billion dollars plan was not approved by the US Senate and therefore GM will not be able to make the payments for its part suppliers by the beginning of the next year. In order to make these payments, GM needs a high amount of liquidity which, at the moment, is not available.

Chrysler is also affected by the Senate's decision, of not approving the plan, after they recently said that without 3 billion dollars they will crash by the end of next year due to the fact that no payments for the part suppliers will be possible.

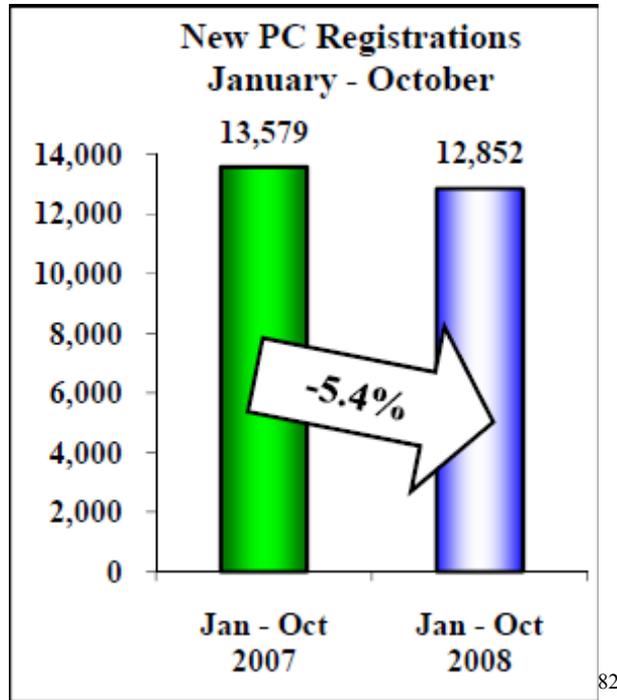
The third US car manufacturer, Ford, which at the moment does not share the fate of its competitors, announced that if GM and Chrysler will go bankrupt they are affected also.

A total surprise concerning the bailout plan, came from the German car manufacturers' federation (VDA), that produce cars in the USA, through the voice of its president. They said that they are just entitled to receive money through the

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bail-out plan, just as much as the other car manufacturers, because otherwise, the American producers would have an advantage that will affect the competition.



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In Europe the new passenger cars registrations reduced by 14,5% only in October. This reduction follows the down going trend for six months, meaning from summer months.

In the Western Europe markets the new cars registrations dropped 15,5% compared to 2007. With the exception of Austria (which had an increase of 4%), all the other important markets fell. The Irish and the Spanish markets continued their sharply downward trend, plummeting -54.6% and -40.0% respectively in October, and down -18.2% and -23.8% over the first ten months of the year. In Spain, registrations in October were the lowest since 1995. In the UK, demand for new cars was down 23.0%, with cumulative results from January to October showing an 8.8% decline. For the tenth consecutive month, new registrations were down on the Italian market (-18.9%), resulting in a 12.0% drop in the cumulative results. In Germany, October new car registrations were 8.2% lower than the already weak result of last year. In France, the market recorded a 7.4% fall. Ten months into 2008, both Germany and France still have a stable number of newly registered cars compared to 2007, recording a +0.3% and +2.2% change respectively over the year onto October.

<sup>82</sup> Source: ACEA (European Automobile Manufacturer's Association)

Registrations of new cars in the Eastern Europe countries also declined in October (-3.2%), with cumulative results holding grounds at a 2.5% plus over the first ten months of the year. The Polish market expanded in October (+12.3%), as well as from January to October (+9.0%), consolidating its position as the largest market in the region. Romania, despite a 10.6% fall in October remained the second biggest market.

	October '08	October '07	% Chg 08/07	Jan - Oct '08	Jan - Oct '07	% Chg 08/07
AUSTRIA	25,992	25,003	+4.0	258,149	256,544	+0.6
BELGIUM	42,998	46,150	-6.8	483,729	464,752	+4.1
DENMARK	11,327	14,533	-22.1	133,219	133,645	-0.3
FINLAND	10,161	11,079	-8.3	128,714	119,767	+7.5
FRANCE	174,939	188,877	-7.4	1,750,703	1,712,238	+2.2
GERMANY	258,814	281,845	-8.2	2,630,287	2,622,337	+0.3
GREECE	19,666	21,088	-6.7	245,902	249,403	-1.4
IRELAND	1,748	3,849	-54.6	150,790	184,394	-18.2
ITALY	167,940	207,049	-18.9	1,879,165	2,134,755	-12.0
LUXEMBURG**	4,488	4,688	-4.3	46,172	44,583	+3.6
NETHERLANDS	41,943	42,251	-0.7	463,015	458,425	+1.0
PORTUGAL	14,678	15,679	-6.4	176,851	170,551	+3.7
SPAIN	77,660	129,384	-40.0	1,025,651	1,345,188	-23.8
SWEDEN	22,299	28,839	-22.7	219,210	248,339	-11.7
UNITED KINGDOM	128,352	166,797	-23.0	1,922,771	2,107,312	-8.8
<b>EUROPEAN UNION (EU15)</b>	<b>1,003,005</b>	<b>1,187,111</b>	<b>-15.5</b>	<b>11,514,328</b>	<b>12,252,233</b>	<b>-6.0</b>
ICELAND	181	1,279	-85.8	8,913	13,727	-35.1
NORWAY	8,390	11,646	-28.0	95,846	109,520	-12.5
SWITZERLAND**	23,379	24,329	-3.9	242,519	237,190	+2.2
<b>EFTA</b>	<b>31,950</b>	<b>37,254</b>	<b>-14.2</b>	<b>347,278</b>	<b>360,437</b>	<b>-3.7</b>
<b>EU15+EFTA</b>	<b>1,034,955</b>	<b>1,224,365</b>	<b>-15.5</b>	<b>11,861,606</b>	<b>12,612,670</b>	<b>-6.0</b>
BULGARIA**	3,878	3,908	-0.8	38,202	33,369	+14.5
CZECH REPUBLIC	12,973	12,120	+7.0	121,973	110,829	+10.1
ESTONIA	1,676	2,533	-33.8	22,202	26,669	-16.7
HUNGARY**	12,879	15,341	-16.0	135,321	144,589	-6.4
LATVIA	1,183	2,632	-55.1	17,239	27,673	-37.7
LITHUANIA	1,715	2,271	-24.5	19,480	17,127	+13.7
POLAND**	27,658	24,630	+12.3	263,462	241,689	+9.0
ROMANIA	24,474	27,371	-10.6	252,924	259,114	-2.4
SLOVAKIA	6,775	5,715	+18.5	58,858	49,194	+19.6
SLOVENIA	5,865	5,882	-0.3	61,120	56,071	+9.0
<b>EU (New Members)</b>	<b>99,076</b>	<b>102,403</b>	<b>-3.2</b>	<b>990,781</b>	<b>966,324</b>	<b>+2.5</b>
<b>EUROPEAN UNION*</b>	<b>1,102,081</b>	<b>1,289,514</b>	<b>-14.5</b>	<b>12,505,109</b>	<b>13,218,557</b>	<b>-5.4</b>
<b>TOTAL EUROPE (EU+EFTA)</b>	<b>1,134,031</b>	<b>1,326,768</b>	<b>-14.5</b>	<b>12,852,387</b>	<b>13,578,994</b>	<b>-5.4</b>

If we talk about brands, Volvo, the Swedish car manufacturer owned today by Ford Motor Company, is expecting that this year's global sales will reach 300.000 units, after selling 458.323 cars in 2007.

The last time when sales dropped below 380.000 was in 1996, when Volvo sold 363.322 cars. Since 1999, when Volvo was bought by Ford, brand sales have

<sup>83</sup> Source: ACEA (European Automobile Manufacturer's Association)

been at around 400.000 units or higher every year. After these sales figures, Ford announced that they will take Volvo into a serious analysis, thinking even about selling it. In US, the sales went down with 29,7% reaching 68.149 sold units from January to November compared with the same period of the last year. Further more in November the sales in US dropped a massive 46,5%, compared with the last year.

BMW, the German car manufacturer, recorded a massive loss in sales figures. Only in November as a result of the crisis they sold 25% less. Due to the fact that the consumers try to reduce their expenditures as much as possible, the German's Group's (which comprises Mini, Rolls-Royce and, of course, BMW) sales reduced 25,4% and the biggest reduction was recorded by BMW brand, that had 26,2% smaller sales.

In contrast with BMW's problems, Audi, another German manufacturer, announced the intention to promote their image at the Super Bowl (the National Football League games in United States) in 2009 after this year's publicity attracted a record number of visitors to its website. Along with Audi, Hyundai Motor America wants to promote its image at this event, also. On the other hand, GM, regular customer of the sporting event, decided not to promote their image.

In Germany, the biggest car market in Europe, the sales are expected to reduce even more till the will reach the levels recorded after the Fall of the Berlin Wall. The recovery is not expected until 2010.

Another European car manufacturer that experiences the financial crisis effects, is Skoda. The Czech producer, now owned by Volkswagen, announced the reduction of the labor week to 4 days, for the first half of 2009. Skoda's sales in Europe went down with 19% in October and the biggest reduction in sales figures was recorded in the Western Europe. Therefore Skoda will stop the production from December 19<sup>th</sup> until January 11<sup>th</sup>, in all the Czech factories reducing its production to 31,000 cars. The manufacturer laid off 1.500 temporary workers were since September, also.

Romania was also affected by this crisis. The national car manufacturer, Dacia, sold 3.710 cars in November, while in October they sold 7.778. As a result of these important reductions, Dacia stopped its production from December 11<sup>th</sup> 2008 until January 11<sup>th</sup> 2009, dismissed 620 temporary employees and reduced the investments for 2009 with 100 million €, from 250 million € to 150 million €. In the same time the part suppliers that work with the Romanian manufacturer will close their factories until January 12<sup>th</sup> 2009.

As a result of this crisis, the Romanian Government announced that the first registration tax will be abolished at least for a year and will apply for the new Euro4 cars that will be purchased. This measure is intended to protect the national car production, so the tax will be increased three times for all second hand imported cars. After Romania waited in vain for a response from the European

Commission regarding this matter, the Prime-Minister decided to apply the modified tax.

This week the Commission said that the tax should be removed for the Euro4 second hand cars that were registered in the EU, from December 15<sup>th</sup> 2008 until December 31<sup>st</sup> 2009 also.

Overall, in October the domestic car producers' sales dropped by 39,5% compared to last year.

The car importers also had important losses starting from September with the top in October when the loss was 25,6% compared to the same period of 2007.

In the same time the registrations for second hand cars increased massively in November at 41.087 cars, which is a record<sup>84</sup>, while the new cars registrations reached the lowest level in the last five years. But APIA<sup>85</sup>'s president, said that the imports of second hand cars, did not increase significantly, only the registration volume did. This is the result of a the rumor that the first registration tax will increase its value, so all dealers that sell second hand imports, wanted to register them.

This tax is calculated taking in consideration the engine displacement among other criteria, which means that the bigger the engine is, the bigger the tax will be. So APIA's president said the tax should be applied only to passenger cars, because the commercial vehicles, are often equipped with large engines.

Even Japan is affected by this crisis. As a result the Japanese car manufacturer will reduce their car production in Japan, Europe and United States of America. So the factory in Japan will produce 40.000 cars less every year. Another measure took by Honda to reduce their costs is the withdrawal from the Formula 1 competitions, as the Formula 1 team had an annual budget of 500 million dollars.

Another Japanese manufacturer that is affected is Nissan that was reevaluated by Fitch Ratings and dropped the qualification from BBB+ to A- because is very dependent to the American market.

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WAYS WOMEN LEAD

Georgiana Cebuc,  
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“Women managers are succeeding today, but they are not adopting the command-and-control style of leadership traditionally practiced by men. Instead, they are drawing on the skills and attitudes they have developed from their experience as women.”

Judy Rosener

Abstract

*Women managers who have broken the glass ceiling in medium-sized, nontraditional organizations have proven that effective leaders don't come from one mold. They have demonstrated that using the command-and-control style of managing others, a style generally associated with men in large, traditional organizations, is not the only way to succeed.*

Keywords: women managers, nontraditional organizations, stereotypes, human relations

JEL classification code: J16, M20, M50.

The role of women worldwide is undergoing a dramatic change. Women today share the podium with men in almost all the fields, be it in kitchen or in defence. Workingwomen are no longer a rarity and are now accepted as an integral part of the working force. Indian organization has experienced a steady increase in the number of women employees and this pattern is bound to continue in the future as well. Women recently began to join the ranks of managers in large number

The first female executives, because they were breaking new ground, adhered to many of the “rules of conduct” that spelled success for men. Now a second wave of women is making its way into top management, not by adopting the style and habits that have proved succesful for men but by drawing on the skills and attitudes they developed from their shared experience as women.

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In a survey sponsored by the International Women's Forum<sup>86</sup>, I found a number of unexpected similarities between men and women leaders along with some important differences. Among these similarities are characteristics related to money and children. I found that men and women respondents earned the same amount of money. This finding is contrary to most studies, which find a considerable wage gap between men and women, even at the executive level. Both married men and women experience moderate levels of conflict between work and family domains.

But the similarities end when men and women describe their leadership performance and how they usually influence those with whom they work. The men are more likely to use power that comes from their organizational position and formal authority. The women respondents, on the other hand, described themselves in ways that characterize "transformational" leadership- getting subordinates to transform their own self-interest into the interest of the group through concern for a broader goal.

### **The Stereotype of Female Managers**

The existence of actual differences between male and female managers has been challenged for some time in the research literature, but strongly held stereotypes are resistant to change. Just how are female managers regarded differently than their male counterparts? In a study by Heilman et al. (1989), researchers asked male managers to characterize both male and female managers. The results indicated a tendency to describe female managers as less self-confident, less emotionally stable, less analytical, less consistent, and having poorer leadership abilities than male managers. Beliefs of this sort contribute to a variety of assumptions about female managers, which in turn form the basis for negative stereotypes about them. Some assumptions typical of a negative stereotype are:

- \* Women tend to place family demands above work considerations. They have children to care for; thus, they lose time for, and interest in, their jobs.

- \* Women work for supplemental income; as a result, they lack the necessary drive to succeed in business.

- \* Women take negative feedback personally rather than professionally. They may run from the room in tears if criticized.

- \* Women are unsuitable for top management positions because they are too emotional and lack aggressiveness.

To some extent, these assumptions may be true for many women in the work force. However, it is questionable whether this negative stereotype accurately

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<sup>86</sup> The International Women Forum was founded in 1982 to give prominent women leaders in diverse professions around the world a way to share their knowledge with each other and with their communities and countries.

describes women who have made the decision to pursue a managerial career. For example, the assumption of family priorities for female executives simply does not apply to many of these women. In a survey of the nation's highest ranked female executives (Baum 1987), nearly half had never married or were divorced, and of those who were married, almost one-third did not have children. Granted, some well-qualified professionals who are mothers may not want the pressure of corporate jobs, but this preference is not true of all or even most female professionals.

### **The Impact of Stereotypes**

Negative stereotypes about women as managers lead to a form of discrimination that is subtle and thus hard to define. Discrimination is seen by many as the "simple-minded sexism of dirty jokes and references to 'girls'," born of hatred and ill will (Fraker 1984). This form of discrimination is blatant and easy to define, and most managers can honestly say they do not discriminate when it is defined in this fashion. However, discrimination also occurs simply by treating women differently from men. People who perceive female managers as different from males often do not realize that they are guilty of discrimination. Instead, differential treatment is seen as logical and rational by those who hold negative stereotypes about women managers.

Subtle discrimination occurs, for example, when a decision is made to offer an important assignment to a man rather than to a woman, based on the assumption that women are not free to take on time-consuming tasks because of family commitments. A related example was provided in a study conducted by Wentling (1992), in which one woman was denied promotion in spite of excellent performance evaluations because her boss felt she would not be with the company very long; he assumed she would probably leave the company to have children. Beliefs about degree of fit also form the basis for subtle discrimination. Women may be excluded from senior management positions because of perceptions that they will somehow change the management process by virtue of their gender. Consider the experience of Barbara Roberts as reported in the Wall Street Journal (Hymowitz and Schellhardt 1986): In the five years Ms. Roberts spent at Dean Witter, she advanced from vice president and coordinator of research services to senior vice president and a member of the securities firm's board .... Then the annual promotions stopped. Instead of being considered for what seemed like the next logical post-executive vice president and director for marketing or research--Ms. Roberts was offered posts she judged to be lateral moves. The explanations she got often sounded blatantly sexist, she says. One man above her in the hierarchy told her "it was his problem, but he couldn't make serious decisions if a woman was in the room."

Across time women have walked the path of traditions. However, in walking these paths, they have made slow but steady departures. As and when the opportunities have come their way and as and when there are challenges thrown their way women, men and organizations have believed that women will not respond. Many women have surprised the world by taking those challenges and working against the odds. In times of crises and in times of immense emotional stress women have risen to the call to take charge of their families, home and destined to give shape to it and move forward. Entering the organizations has been a formidable challenge. Moving from infrastructural roles of the sixties and rising to managerial roles and responsibilities which is almost a Herculean task, and rising into senior management position is an uphill struggle. For women to occupy the position of CEO's in the present scenario, which was a rarity and almost impossibility, today is a reality.

### **External environment**

The external environment has created the universalisation of education and the government has formulated policies to encourage the girl child for higher education. The educational institutions facilitated women to discover their competencies and achieve and succeed.

The external environment provides women the awareness and opportunities of career and occupation. Men simultaneously compete for these opportunities. In a fair for all arenas of job markets, women bring to the organization their education, their achievements and competence their determination and resilience. With this they also bring their doubts, emotional vulnerabilities and fragilities, which become the hallmark for women. Caught between competence and doubts, achievements and roadblocks of guilt and success and anxieties, women carry a unique juxtaposition of determination and ambivalence about breaking new paths and taking new roles.

### **Internal environment**

The internal environment of women consists of parental home and their own home, the society, neighborhood and community as well as the internal dynamics of the work place.

Having entered the organization and having successfully competed with the male world, women encounter the labels of preferred treatment, having a godfather or using femininity as a means of entry. Having entered the organization in managerial positions with responsibility and authority, there are allegations of women entering the position through quota system and not merit. Women respond to these with some defiance, some defensiveness and some selfprotection only to be labeled as insecured, unprofessional. By and large, the women are undervalued

by the system. If her capabilities and competencies are accepted, respected and translated into operational roles, she creates anxieties, hostilities and aggression in others<sup>87</sup>.

Similarly, in the home setting women are propelled to be educated, pulled to stay at home, pushed to take jobs to enhance the quality of life and condemned and accused for not playing their social roles. At another level, there is recognition of their achievements, supported to excel and encouraged to be professionals.

Women themselves accept that they have other meanings in life besides only the social roles and they have an internal evocation to enlarge their life space through commitment to growth.

Put together, the external and internal environment create opportunities and challenges as well as roadblocks to growth. These are present in varied intensities and it is up to the women to carve out a road map and niche for themselves.

Major roadblocks for women who aspire to achieve and succeed in organizations are the presence of social and role of constraints imposed upon them by society, the family and women themselves. These constraints, are referred as myths fostered and sustained with preconceived ideas and unsupported evidence, which generate guilt in women.

Another spectrum of women not gaining the managerial position is because of three categories of behavior habits and styles of operating

- ✚ Women managers are not given high risk, high profile assignment necessary for promotions, because on the way up the ladder they are cautious and avoid taking risks. Women are more cautious and more likely than men to reflect rather than to act.

- ✚ Women concern for others and sense of responsibilities for the team can make them too detail oriented 'moving them into a rescuing and mothering mode and not leaving time for managing the broader challenges.

- ✚ Women who had to be tough and even righteous about their agendas in mid-level positions find these characteristics are hard to shake when they reach to the top level. They become defensive about challenges to their ideas or agendas and too insecure to think and interact with creative flexibility.

Women manager needs to establish their career goals and acquire determination to overcome the obstacles that exist to keep women from

accomplishing their goals. However, in order to overcome such insurmountable obstacle, women need to seek support. Success today requires organizations to best utilize the talent available to them irrespective of the gender. To do these, barriers to upward mobility for women needs to be removed. Organizations need to redefine and restructure the organization systems to respond to the dilemmas faced by women managers. Organization has recognized

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<sup>87</sup> Indira J Parkikh, "*Women Managers From Myths To Reality*", Indian Institute of Management, 2003

that female executives offer a wealth of talent. Often women become ‘*Super Woman*’ to respond to being equal. The striking part of women managers is that they are very good at juggling around the tasks. One of the strongest skills is their ability at multi-tasking. Also women managers bring with them a different style and different skills. Research also confirms that women managers see things laterally, intuitively and differently. They can handle more contradictions, can tolerate more and deliver much more than men.

The belief that women managers are uncertain of themselves, look for constant

reassurance and tend to be aggressive are stereotyped responses which feed and multiply on themselves. The reality is that women in general and women managers in particular have a different value system, which they bring to the organization.

Women managers and women in leadership roles are today a reality. The momentum will continue and the chains will break and the shackles will fall. The glass ceiling will shatter and the women will bring a tempering of the masculine organization structure with gentler and softer human processes<sup>88</sup>

Time will come to pass when women will bring creativity and innovativeness and men will join to make it a reality. It is the rhythm of the two polarities that a new order organization would be created. Work will pull the best resource and not the gender specific response or gender stereotypical response.

### **Situation of women managers in Europe**

To understand what the labyrinth involves for working women in Europe, the Fourth European Working Conditions Survey 2005 (4th EWCS) provides empirical evidence. This survey gives a wealth of information on the conditions of work and employment in 31 European countries. The EWCS is based in a multi-stage stratified random sample, representative of the EU working population (Eurofound, 2007). For the purposes of this report, we will use a subsample including only employees working in establishments with at least two employees and we limit the description to workers in EU27 countries; this accounts for more than 21,200 cases.

The data on female managers in the European countries can be looked at from two perspectives. On the one hand, we will describe those women who state that they have a supervisory position, while on the other hand, we will also look at it from the other angle, using information on the employees who say they have a female boss. The 4th EWCS allows this two-pronged approach, since the

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<sup>88</sup> Voros, Sharon; Woman Managers must meet high expectation; Career Journal from the Wall Street Journal; 2003.

respondents are asked both if they are in a supervisory position and if they have a female or male boss.

The two approaches complement each other, as the descriptive analysis of women managers and subordinates of female bosses interact with each other. The relationship also reflects the gendered division of labour in the European Union.

Just to give one example, women managers tend to work in health and education sectors and their subordinates tend to be women. To obtain the full picture, we will first describe female managers themselves and then turn our attention to the characteristics of the subordinates of female bosses, i.e. those that indicate in the survey that 'their immediate boss' is a woman.

### **Female managers**

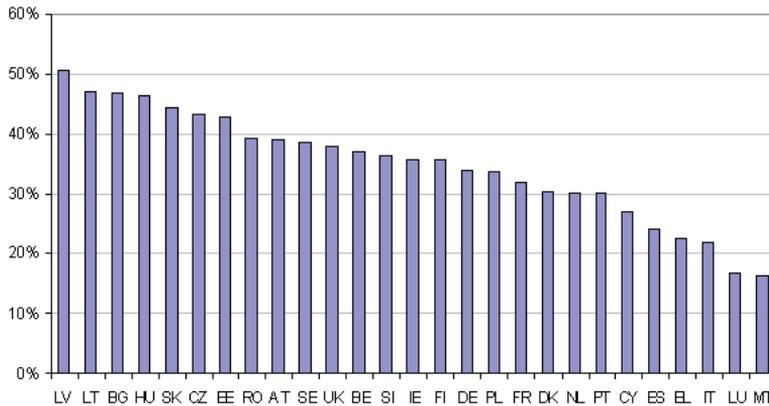
In Europe, 33% of managers were women in 2005. The figure describes the proportion of women among the employees who state that they have people working directly under their supervision. Numbers drawn from the survey are in line with the statistics provided by the ILO (2004) stating that in the period 2000 to 2002, the proportion of women in managerial jobs was 20% to 40% in 48 countries.

Still, the numbers are worth looking at in more detail, since there are very large differences in the incidence of women managers according to country (Figure 1). In Latvia, gender equality, as measured by the number of female bosses, seems to have been reached, as the proportion of women managers is 51%. Other Eastern European countries are also close to achieving gender equality in respect of numbers of women managers, with the proportions above 40% in most of the Eastern European countries.

As for Romania, it is interesting to notice that one of the most important businessmen, Ion Tiriac, has chosen Anca Ioan last year, to run his businesses which exceed 1 billion Euros yearly. Ted Lattimore, ex COO of Connex, who was taken by Vodafone in 2006, declared when he took his position in 2000, that he was surprised by the large number of women working for Connex, many of them in higher positions. Not as irony, he was replaced in 2005, by a Romanian woman, Liliana Simion.

In Continental Europe and Scandinavia, the proportions of women managers are close to the EU average, with percentages around 30% to 40%. In Southern Europe, the share of female bosses is modest. For example, in Malta, only 16% of bosses are women. Luxembourg has a place among the Southern European countries as regards the proportion of female managers, where only 17% of bosses are women.

Figure 1: *Women managers by country*

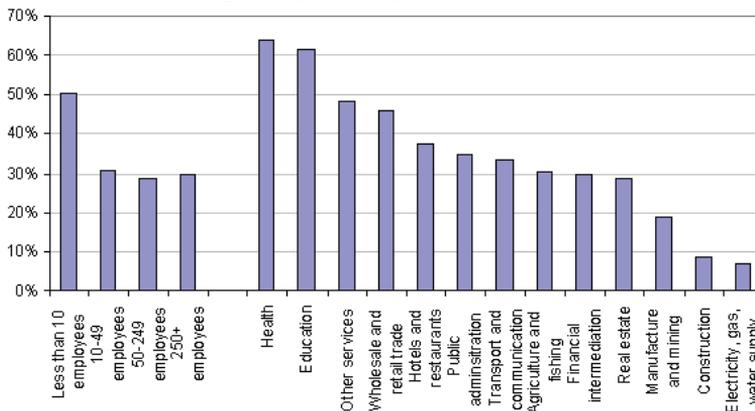


Source: *EWCS (2005)*.

As was suggested before, women managers are concentrated in certain types of establishments and sectors, thereby highlighting the gendered division of labour (Figure 2). In micro enterprises, where the number of employees is fewer than 10, the share of male and female managers is equal: half of the managers in micro enterprises are women. However, in bigger establishments, the share of women in supervisory roles is around 30%.

Gender segregation in the labour market is quite clear as far as managerial positions are concerned. Women managers are overrepresented in the health and education sectors, where the shares of women top are over 60%. Female managers are also often found in other services and wholesale and retail trade sectors, as over 40% of managers working there are women. Unsurprisingly, women managers are only rarely found in traditionally male work environments such as manufacture and mining, construction and electricity, gas and water supply sectors.

Figure 2: *Women managers by size of establishment and sector*

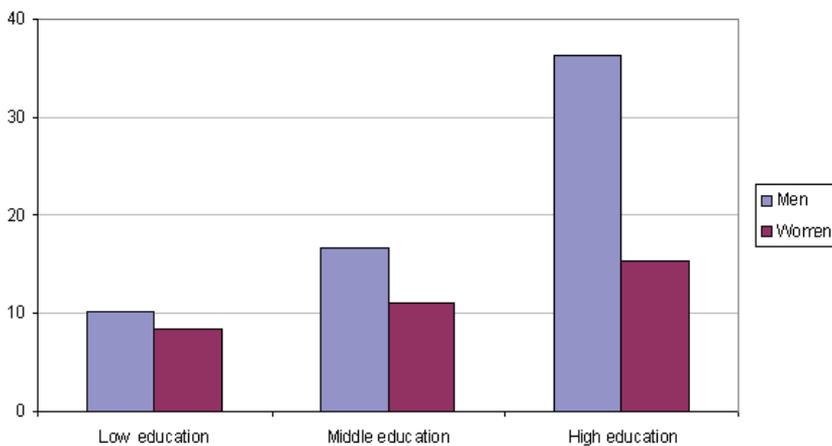


Source: *EWCS (2005)*.

When describing the incidence of female managers, it is also important to pose the question of how men and women become managers. Do they have different kinds of career paths, as the literature suggests, and if they do, where do the differences lie? The answers to these questions shed some light on the process of achieving gender equality.

The shares of employees in managerial positions increase with education for both men and women. However, the returns of a higher education are greater for men than for women as far as attaining managerial positions is concerned (Figure 3). Some 36% of highly educated men work as managers, whereas the proportion of highly educated women having a managerial position is more than two times smaller, at only 15%.

Figure 3: *Share of male and female managers by level of education (%)*



Source: *EWCS (2005)*.

As it usually takes time to advance in a career, to attain a high level of education as well as to reach a managerial position, it is not surprising that less than 10% of 15–29-year-old employees are managers. Within the cohort of 30–49-year-olds, the share of managers increases significantly for men but not for women: 23% of men in this age group work as managers, compared to 13% of women.

There are still considerably fewer women than men in managerial positions in Europe, even if the findings show that the gender ‘management gap’ is closing at a steady (and slow) pace. Two other significant issues we have identified in this report are a high degree of occupational segregation of female bosses (as much as for female employment in general) and the fact that women in managerial positions tend to be in lower hierarchical levels than men.

Many of the structural barriers women might face on their way to top-level positions have been removed, for example by introducing policies that support

gender equality and combat discriminatory practices. This has shifted the focus onto cultural barriers. The most recent literature discussing male and female leaders pays attention to subjective aspects such as stereotypes and gender roles. In this report, we have tried to find evidence of systematic differences in leadership styles between men and women by looking at the impact these styles would have on psychosocial conditions at the workplace as reported by subordinates of male and female bosses.

The analysis has shown that there are no significant differences between male and female bosses for most areas of human relations at the workplace that we have covered (communication with and support from superiors, autonomy at work,

work intensity). It seems that it is usually the subordinate's gender that makes a difference, rather than the boss's gender, for example, with female workers declaring less communication with the boss and less autonomy at work compared to male workers. The only clear indication that male and female managers might create different working conditions was found at the level of the psychological work environment. The results point out that subordinates of female bosses report slightly higher levels of bullying and harassment and slightly lower levels of job satisfaction than those who are supervised by a man. Not finding a correlation can prove that a causal relation does not exist (it is very unlikely that we would have missed it), but finding a correlation does not prove that a causal relation exists, as there may be other unobserved factors explaining the correlation. This is what happens with the interesting, but difficult to explain, relationship found between the boss's gender and bullying and harassment and satisfaction with working conditions. Furthermore, this relationship is not consistent in all the country clusters, which suggests that there are probably some culturally determined factors behind it. This is definitely an issue that requires further research, probably with a methodology that is more sensitive to the cultural construction of gender and managerial models. With the methods used here, we can only point to some potential explanations to this (still to be consistently proven) finding.

We controlled for occupation and sector in the workplace, which reduces some of the variability resulting from the segregation by gender in the labour market. But we did not control by the supervisory level of male and female bosses, which, as we argued earlier, are quite different. Female bosses are more often in low levels of hierarchy, and this may imply that in their positions, the levels of bullying and harassment may be higher, or that they may have less authority to intervene in cases of bullying (see Hurley and Riso, 2007)

In addition, the psychological work environment may suffer if the manager is not perceived as suitable for her position. This might happen when gender and manager roles are not perceived as fitting, which according to the literature is more likely to happen for women managers (as a result of the double bind). Researchers who have studied bullying and harassment at the workplace suggest

that the manager has a significant impact on the psychological working environment and that bullying often arises in conflict situations and in cases of role conflict and ambiguity (e.g. Ayoko et al., 2003; Matthiesen and Einarsen, 2007)<sup>89</sup>.

Overall, analysis suggests that it is not gender that makes men or women better suited for managerial positions, but rather, subtle conflicts and interactions between stereotypes of men, women and managers make it either easier or more difficult to act successfully as a manager. These stereotypes are culturally constructed and changeable. As it is shown, gender equality in working life has not been reached yet. In Europe, many of the concrete obstacles for women to advance in their career have been successfully removed. A necessary further step is to also acknowledge the possible gender bias when addressing and fulfilling managerial positions, and even when working for a female boss.

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