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ОПШТИНСКИТЕ ОБВРЗНИЦИ КАКО РЕШЕНИЕ НА ЕДЕН ОД ПРОБЛЕМИТЕ НА ЛОКАЛНАТА ДЕМОКРАТИЈА *1*

PhD Candidate Nuhi SELA

DYNAMICS OF PRODUCTION FOR THE ENTERPRISES WITH PRIVATE OWNERSHIP: CASE STUDY *15*

М-р Емануела ЕСМЕРОВА

СТРАТЕГИСКИ МЕНАЏМЕНТ , МОДЕЛИ, ПЛАНОВИ И СТРАТЕГИИ *29*

Проф. д-р Лидија НАУМОВСКА, М-р Верица НЕДЕЛКОВСКА

ИНКЛУЗИВНОСТ НА ИНВАЛИДИТЕ ВО МАКЕДОНСКИТЕ КОМПАНИИ *45*

М-р Јасмина МИШОСКА

ОХРАБРУВАЊЕ НА ПРЕТПРИЕМАЧКИОТ ДУХ ЗА КАРИЕРЕН РАЗВОЈ ...*63*

Доц. д-р Елизабета СТАМЕВСКА

ПРИМЕНАТА НА ДОБРО КОРПОРАТИВНО УПРАВУВАЊЕ – НЕОПХОДНОСТ ЗА ОДРЖЛИВ ЕКОНОМСКИ РАСТ НА КОМПАНИИТЕ..*73*

М-р Емилија МИТЕВА - КАЦАРСКИ, М-р Костадинка ЧАБУЛЕБА

ЕКОНОМИЈА БАЗИРАНА НА ЗНАЕЊЕ - ГЛОБАЛНИ ТРЕНДОВИ И ИМПЛИКАЦИИ *86*

M.Sc. Mitko VELJUSLIEV, M.Sc. Aleksandar NACEV, Kire NIKOLOVSKI

MANAGEMENT - SCIENCE AND SKILL..*97*

Елизабета ТРАЈАНОВСКА СРБИНОСКА

ИНТЕРНЕТ ПАРИ – БЕЗБЕДНОСТ ПРОЦЕНКА И ИНОВАЦИИ *106*

Проф. д-р Маријан СТЕВАНОВСКИ

ВЛИЈАНИЕТО НА РЕВЕРЗИБИЛНИ ЕФЕКТИ НА ФИНАНСИСКАТА КРИЗА И ГЛОБАЛИЗАЦИЈАТА ВРЗ ОПШТЕСТВЕНИОТ РАЗВОЈ............................*119*

Д-р Лазар ЃУРОВ, М-р Кемо ЃОЗО, Стефан ПЕЈОВСКИ

ВЛИЈАНИЕТО НА ЕМОЦИОНАЛНАТА ИНТЕЛИГЕНЦИЈА ВРЗ ОСТВАРУВАЊЕТО НА УСПЕШНА КОМУНИКАЦИЈА НА ЛИДЕРИТЕ *133*

М-р Кемо ЃОЗО, Д-р Лазар ЃУРОВ, Филип АЛЕКСОВСКИ

УЛОГАТА НА КОМУНИКАЦИСКИТЕ ВЕШТИНИ НА ЛИДЕРИТЕ ВО УСПЕШНОТО РАБОТЕЊЕ СО ПОТЧИНЕТИТЕ И ПРЕТПОСТАВЕНИТЕ*153*

Проф. д-р Александра СТАНКОВСКА

РАЗВОЈ НА ПАЗАР ЗА ФИНАНСИСКИ ДЕРИВАТИ – ПЛАТФОРМА ЗА УПРАВУВАЊЕ СО ПАЗАРНИ РИЗИЦИ...*176*

Проф. д-р Живко АНДРЕВСКИ

ДЕСЕТ ТЕМИ ЗА ПРОМОЦИЈА НА НАУКАТА ВО РЕПУБЛИКА МАКЕДОНИЈА
....*198*

Доц. д-р Лулзиме ЛУТВИУ КАДРИУ, М-р Беким КАДРИУ

МЕНАЏЕРСКОТО ОБРАЗОВАНИЕ КАКО СТРАТЕГИЈА ЗА ПРОМЕНИ ВО УЧИЛИШТЕТО *209*

Проф. д-р Савица ДИМИТРИЕСКА, Проф. д-р Љиљана КОНЕСКА

ЗЕЛЕН МАРКЕТИНГ И ОДДРЖЛИВ РАЗВОЈ *224*

Проф. д-р Савица ДИМИТРИЕСКА

НЕВРОМАРКЕТИНГ – ВРСКА ПОМЕЃУ НАУКАТА И БИЗНИСОТ *237*

Assistant prof. Biljana PETREVSKA

ESTIMATING TOURISM CONTRIBUTION TO MACEDONIAN ECONOMY..*248*

М-р Тања КАУРИН

КОНЦЕПТОТ НА ЛИКВИДНОСТА ВО БАНКАРСКАТА ТЕОРИЈА И ПРАКТИКА...*261*

М-р Биљана ТРАЈКОВСКА

ИНТЕРНЕТОТ ВО ФУНКЦИЈА НА ОПШТЕСТВЕНИОТ РАЗВОЈ.................*286*

Бојан ШАЈНОСКИ

ОДЛУЧУВАЊЕТО И ИНТЕРЕСИТЕ *304*

М-р Тане ДИМОВСКИ

ИНТЕРВЈУТО КАКО ПРОЦЕС ОД МЕНАЏМЕНТОТ НА ЧОВЕЧКИТЕ РЕСУРСИ НА ОРГАНИЗАЦИЈА *313*

Д-р Ристо ФОТОВ, М-р Влатко ПАЧЕШКОСКИ

НЕКОИ АСПЕКТИ ЗА ВЛИЈАНИЕТО НА ТЕХНОЛОШКИОТ НАПРЕДОК И ИНОВАЦИИТЕ ВРЗ ЕКОНОМСКИОТ РАЗВОЈ...*323*

Assistant prof. Vesna GEORGIEVA SVRTINOV, PhD Riste TEMJANOVSKI, Assistant prof. Janka DIMITROVA

GLOBALIZATION AND THE INCOME DISTRIBUTION BETWEEN THE COUNTRIES...*334*

Assistant prof. Olivera GJORGIEVA - TRAJKOVSKA, Assistant prof. Janka DIMITROVA, Assistant prof. Aleksandar KOSTADINOVSKI

THE IMPLICATIONS OF GLOBAL FINANCIAL CRISIS ON DEVELOPING COUNTRIES-WITH SPECIAL REFERENCE TO MACEDONIA *347*

Д-р Ирена АНДРЕЕСКА

ЕКОНОМСКА НЕЕДНАКВОСТ КАКО ПРОИЗВОД НА ГЛОБАЛИЗАЦИЈАТА *367*

Д-р Александар КОСТАДИНОВСКИ, Д-р Оливера ЃОРГИЕВА ТРАЈКОВСКА, М-р Благица КОЛЕВА

ФАКТОРИТЕ НА ВЛИЈАНИЕ ВРЗ ПЕРФОРМАНСИТЕ НА ЗДРАВСТВЕНАТА РАБОТНА СИЛА..*377*

М-р Драгана ЛАЗАРЕВСКА

НЕВРАБОТЕНОСТА ПРИЧИНИТЕЛ ЗА ЗГОЛЕМУВАЊЕ НА СИРОМАШТИЈАТА ВО РЕПУБЛИКА МАКЕДОНИЈА....................................*390*

М-р Тања КРСТЕВА

КОМПОНЕНТИ НА МОДЕРНИОТ МАРКЕТИНГ ИНФОРМАЦИОНЕН СИСТЕМ *409*

М-р Тања КРСТЕВА, М-р Елена КОНЕСКА-ИЛИУ

АСПЕКТИ НА ИНФОРМАЦИОНИОТ СИСТЕМ ЗА ПЛАНИРАЊЕ (ЕРП)...*420*

М-р Елена ПАГОВСКА, М-р Милена ПАГОВСКА

ФИНАНСИРАЊЕ НА КАПИТАЛНИТЕ ИНВЕСТИЦИИ ВО ОПШТИНИТЕ НА РЕПУБЛИКА МАКЕДОНИЈА ПРЕКУ ЈПП..*431*

M.Sc. Milena PAGOVSKA

CONSUMER ETHNOCENTRISM AMONG MACEDONIAN CONSUMERS AND ITS EFFECTS ON THE PURCHASE DECISION *447*

M.Sc. Daniela KOTESKA LOZANOSKA, M.Sc. Goran SHIBAKOVSKI

HUMAN RESOURCES AND ECONOMIC DEVELOPMENT...............................*464*

М-р Анита СКРЧЕСКА

ПРЕДИЗВИЦИТЕ НА СМЕТКОВОДСТВОТО НА МЕНАЏМЕНТОТ ПРИ УТВРДУВАЊЕТО НА ИНТЕРНИТЕ ЦЕНИ ВО МУЛТИНАЦИОНАЛНИТЕ ПРЕТПРИЈАТИЈА ВО УСЛОВИ НА ЕКОНОМСКА КРИЗА............................*477*

М-р Верица НЕДЕЛКОВСКА, М-р Елена НАУМОВСКА

ГРАДЕЊЕ БИЗНИС СТРАТЕГИИ СО ПРИМЕНА НА АНАЛИТИЧКА И КРЕАТИВНА СПОСОБНОСТ..*490*

М-р Шкодране ДАРДИШТА, М-р Верица НАЈДОВСКА

ПЕРСПЕКТИВА И ПРОГНОЗИ ЗА ПОДОБРУВАЊЕ НА КВАЛИТЕТОТ НА РАБОТАТА НА ЈАВНАТА УСТАНОВА ВО КОМПЛЕКСОТ НА ЗДРАВСТВЕНИОТ СЕКТОР *504*

Доц. д-р Александра АНДРЕСКА САРЕВСКА, М-р Верица НАЈДОВСКА

КОРИСТ И БАРИЕРИ ПРИ СПРОВЕДУВАЊЕ НА ONLINE БИЗНИС...........*512*

Проф. д-р Алекса СТАМЕНКОВСКИ

УЛОГАТА НА МАРКЕТИНГОТ ВО ЕКОНОМСКИОТ РАЗВОЈ......................*520*

Д-р Весна ГРОЗДАНОВСКА

ИНДУСТРИСКИОТ МЕНАЏМЕНТ И ЕКОНОМСКИОТ РАЗВОЈ *530*

М-р Мирослав МИТРОВСКИ

МЕЃУНАРОДНИТЕ ФИНАНСИСКИ ТЕКОВИ И ЕКОНОМСКИОТ РАЗВОЈ НА РЕПУБЛИКА МАКЕДОНИЈА..*540*

Д-р Иван ИГЊАТОВ

ВАЖНОСТА НА СОЦИЈАЛНАТА РЕВИЗИЈА КАКО АЛАТКА ЗА ЗГОЛЕМУВАЊЕ НА ОТЧЕТНОСТА И ТРАНСПАРЕНТНОСТА ВО РАБОТЕЊЕТО..*553*

Деан КОЦЕВСКИ, Д-р Иван ИГЊАТОВ

ВАЖНОСТА НА СТРАТЕШКИОТ ПРИСТАП ПРИ ИМПЛЕМЕНТИРАЊЕ НА СИСТЕМ ЗА МЕНАЏИРАЊЕ НА ДОКУМЕНТИ ЗА ЗГОЛЕМУВАЊЕ НА ЕФЕКТИВНОСТА НА РЕВИЗОРСКИТЕ АКТИВНОСТИ *567*

PhD Ljubo PEJANOVIC

COORDINATED PREVENTION AND SUPPRESSION CRIME IN MACEDONIA AND REPUBLIC OF SERBIA..*582*

Доц. д-р Билјана ТОДОРОВА

ПРАВО НА СТРАНЦИТЕ ДА СТАПУВААТ ВО РАБОТНИ ОДНОСИ ВО РЕПУБЛИКА МАКЕДОНИЈА...*593*

Марија СРБИНОВСКА

ПРЕТРЕС...*610*

Доц. д-р Рабије МУРАТИ

КОНЦЕПТУАЛНА РАМКА НА ДЕМОКРАТИЗАЦИЈАТА НА ОБРАЗОВАНИЕТО

....*619*

Докторант Фатон ШАБАНИ

ИСКЛУЧОЦИТЕ ОД ПАТЕНТНА ЗАШТИТА СПОРЕД ЗАКОНОТ ЗА ИНДУСТРИСКА СОПСТВЕНОСТ НА РЕПУБЛИКА МАКЕДОНИЈА...........*632*

М-р Валдета ЗАНУНИ-ИДРИЗИ, М-р Афрдита ИЛАЗИ-ХОЏА

ФОРМАТИВНОТО ОЦЕНУВАЊЕ ВО ФУНКЦИЈА НА ГРАДЕЊЕ НА ДОБРИ ОДНОСИ МЕЃУ УЧЕНИЦИТЕ И НАСТАВНИЦИТЕ И НЕЈЗИНОТО ВЛИЈАНИЕ ВРЗ ПОСТИГАЊАТА НА УЧЕНИЦИТЕ *645*

Проф. д-р Слободан ШАЈНОСКИ

ПРИВАТИЗАЦИЈАТА И АКЦИОНЕРСКАТА СОПСТВЕНОСТ *660*

Проф. д-р Живко АНДРЕВСКИ, Доц. д-р Билјана ТОДОРОВА

ПРЕДИЗВИЦИТЕ НА ПРАВНАТА НАУКА ВО РЕПУБЛИКА МАКЕДОНИЈА

....*671*

Прод. д-р Виолета НИКОЛОВСКА

ИНТЕРДИСЦИПЛИНАРНОСТА ВО НАУКАТА И ЛИНГВИСТИКАТА *683*

М-р Росана ЈАНЕВСКА

КАЗНЕНО – ПРАВНИ И МОРАЛНО – ЕТИЧКИ АСПЕКТИ НА КЛОНИРАЊЕТО..*696*

Д-р Македонка РАДУЛОВИЌ

ИДНИНАТА НА НАУКАТА ЗА СЕМЕЈСТВОТО ВО РЕПУБЛИКА МАКЕДОНИЈА

....*714*

Доц. д-р Ивица МАКСИМОВСКИ

ИНВЕСТИРАЊЕ ВО ОБРАЗОВАНИЕТО И НАУКАТА *732*

М-р Марјан ГАБЕРОВ

ТРАНСНАЦИОНАЛЕН ОРГАНИЗИРАН КРИМИНАЛИТЕТ...........................*750*

Далина НАЌЕВА-ПОТУРАК

ПРАВНА РАМКА ЗА ФУНКЦИОНИРАЊЕ НА МИНИСТЕРСТВОТО ЗА ВНАТРЕШНИ РАБОТИ НА РЕПУБЛИКА МАКЕДОНИЈА *765*

Александар КРСТЕВСКИ

ЕВРОПСКАТА УНИЈА КАКО СУБЈЕКТ НА МЕЃУНАРОДНОТО ПРАВО *.782,*

Проф. д-р Владо ВАНКОВСКИ, Дијана АНГЕЛЕСКА

МОРАЛНА РЕЦЕСИЈА НА НАУКАТА-СТОМАТОЛОГИЈАТА ДЕНЕС *796*

Доц. д-р Елизабета СТАМЕВСКА, Антониела СТАМЕВСКА

АСПЕКТИ НА СИСТЕМОТ ЗА ОБЕЗБЕДУВАЊЕ КВАЛИТЕТ ВО ВИСОКОТО ОБРАЗОВАНИЕ *810*

Душко ПЕТРОВ

ГЛАСАЧКО ОДНЕСУВАЊЕ ВО РЕПУБЛИКА МАКЕДОНИЈА......................*821*

M.Sc. Afrodita NIKOLOVA

A READER-RESPONSE DISCUSSION OF "ANGEL LEVINE" BY MALAMUD: DOES READING REALLY CHANGE US FOR THE BETTER?............................*837*

Проф. д-р Драге ПЕТРЕСКИ, Проф. д-р Ненад ТАНЕСКИ, Проф. д-р Андреј ИЛИЕВ

ИСПОРАКИТЕ НА ОРУЖЈЕ НА ЗЕМЈИТЕ ВО РАЗВОЈ *858*

М-р Александар НАЦЕВ, М-р Митко ВЕЉУСЛИЕВ

БЕЗБЕДНОСНИТЕ АСПЕКТИ НА РАЗВОЈОТ НА ОПШТЕСТВОТО............*876*

Проф. д-р Методија ДОЈЧИНОВСКИ

ПРИМЕНА НА РАЗУЗНАВАЧКАТА ДЕЈНОСТ ПРИ СПРОВЕДУВАЊЕ НА МИСИИТЕ НА ВОЕНИТЕ АТАШЕА *888*

Проф. д-р Андреј ИЛИЕВ, Проф. д-р Драге ПЕТРЕСКИ, М-р Драган ЃУРЧЕВСКИ, Трајче ДЕНЧЕВСКИ

ЕВОЛУТИВЕН РАЗВОЈ НА МИСИЈАТА ИСАФ НА НАТО И НЕЈЗИНИТЕ ИДНИ ИМПЛИКАЦИИ ВРЗ ГЛОБАЛНАТА БЕЗБЕДНОСТ.............................*906*

Доц. д-р Викторија КАФЕЏИСКА

РАЗЛИКИТЕ МЕЃУ НАЦИОНАЛНОТО И МЕЃУНАРОДНОТО ОПШТЕСТВО - ОРГАНИЗАЦИЈА НА МОЌТА..*932*

М-р Филимена ЛАЗАРЕВСКА

МЕНТАЛНОТО РАСТРОЈСТВО F22 КАКО ГЛАВЕН ИНДИКАТОР ЗА ПРИЧИНСКО ПОСЛЕДИЧНА ПОВРЗАНОСТ НА КРИМИНОГЕНОТО ОДНЕСУВАЊЕ...*944*

М-р Стефанија АГРОТОВА

ВЛИЈАНИЕТО НА ЕТНИЧКАТА РАЗЛИЧНОСТ ВРЗ РАЗВОЈОТ НА ОПШТЕСТВОТО

....*963*

Проф. д-р Слободанка ТОДОРОСКА-ЃУРЧЕВСКА

СТРУКТУРНИТЕ ЕЛЕМЕНТИ НА ЕМОЦИОНАЛНАТА ИНТЕЛИГЕНЦИЈА

....*975*

Проф. д-р Стојан СЛАВЕСКИ

РЕФОРМИТЕ НА БЕЗБЕДНОСНИОТ СИСТЕМ НА РЕПУБЛИКА МАКЕДОНИЈА: ОД СЕГМЕНТИРАН ДО ИНТЕГРИРАН БЕЗБЕДНОСЕН СИСТЕМ?

....*996*

Фатмир ИБИШИ

КРИВИЧНОТО ДЕЛО "КРИУМЧАРЕЊЕ НА МИГРАНТИ" ВО РЕПУБЛИКА МАКЕДОНИЈА..*1014*

Д-р Фердинанд ОЏАКОВ, Проф. д-р Атанас КОЗАРЕВ, Мирјана МАНЕВСКА

УЛОГАТА НА БЕЗБЕДНОСНИТЕ СЛУЖБИ ВО СПРАВУВАЊЕТО СО ПСИХОЛОШКО-ПРОПАГАНДНИТЕ ДЕЈСТВА – КЛУЧЕН ФАКТОР ВО ОДБРАНАТА НА НАЦИОНАЛНАТА БЕЗБЕДНОСТ НА ДРЖАВАТА.........*1029*

Александар ТРАЈКОВСКИ

ИМПЛИКАЦИИТЕ НА ГЛОБАЛИЗАЦИЈАТА ВРЗ ПОДЕМОТ НА ОРГАНИЗИРАНИОТ КРИМИНАЛ ВО 21-ОТ ВЕК...*1047*

Проф. д-р Душко СТОЈАНОВСКИ, М-р Саит САИТИ

ОДГОВОРНОСТ НА РАБОТНИЦИТЕ ЗА ПРИВАТНО ОБЕЗБЕДУВАЊЕ – СО ПОСЕБЕН ОСВРТ НА ПРЕКРШОЧНАТА ОДГОВОРНОСТ *1059*

M.Sc. Jovica MIJALKOVIC, PhD Petar NAMICEV

СОВРЕМЕНАТА УРБАНИЗАЦИЈА И ВЛИЈАНИЕТО ВРЗ СОВРЕМЕНИОТ КОНЦЕПТ НА ГРАДОТ...*1076*

Проф. д-р Петар НАМИЧЕВ

ВЛИЈАНИЕТО НА СОВРЕМЕНАТА УРБАНИЗАЦИЈА ВРЗ КОНЦЕПТОТ НА ЖИВЕАЛИШТАТА..*1092*

M.Sc. Valentina PAJAZITI, M.Sc. Mensur PAJAZITI

FASHION AND DESIGN AS THE CHALLENGE IN SCIENCE..........................*1107*

М-р Марина КОЦАРЕВА РАНИСАВЉЕВ

НАУКАТА И УМЕТНОСТА ВО ВИЗИЈАТА НА ПОСТМОДЕРНИТЕ ДИЗАЈНЕРИ

....*1116*

Мимоза КЛЕКОВСКА, Цвета МАРТИНОВСКА

ХАРМОНИСКИТЕ ПРОПОРЦИИ КАКО БИТЕН ЕЛЕМЕНТ ВО ПРЕПОЗНАВАЊЕТО НА СТИЛСКИТЕ ОСОБЕНОСТИ КАЈ ФОРМИТЕ ОД ЦРКОВНОСЛОВЕНСКАТА АЗБУКА *1137*

PhD Aleksandra STANKOVSKA, M.Sc. Jovica MIJALKOVIC

ARCHITECTURAL DESIGN AND REAL ESTATE VALUES ....

1166

М-р Стојанка МАНЕВА-ЧУПОСКА - ЈАНА, Елена МАКАРОСКА

ВЛИЈАНИЕТО НА СОВРЕМЕНАТА УРБАНИЗАЦИЈА ВРЗ УМЕТНОСТА

....*1193*

MA Gordana VRENCOSKA

THE PROSPECTS OF INCLUSIVE DESIGN IN THE MACEDONIAN CIVIL SOCIETY

....*1209*

Цветлана ТАСЕВСКА, Марјана АНДРИЈЕСКА, Проф. д-р Ристо ХРИСТОВ

КРИПТОГРАФСКА ЗАШТИТА НА БАЗА НА ПОДАТОЦИ...........................*1226*

Катерина МИТКОВСКА-ТРЕНДОВА, Проф. д-р Росе СМИЛЕСКИ

РЕАЛНОСТА, ЕКСПЕРИМЕНТОТ И МАТЕМАТИЧКИОТ МОДЕЛ *1239*

PhD Biljana PERCHINKOVA, PhD Andrej CVETKOVSKI, PhD Irena PLETIKOSA CVIJIKJ

SOLVING SYSTEMS OF NONLINEAR EQUATIONS BY DIMENSIONALITY AUGMENTATION..*1251*

Зорица КАЕВИЌ, Д-р Сашо ГЕЛЕВ, Проф. д-р Атанас КОЗАРЕВ

ФОРЕНЗИКА НА USB И COMPACT FLASH МЕМОРИСКИ УРЕДИ *1264*

1153 М-р Стојанка МАНЕВА-ЧУПОСКА - ЈАНА **СЛОБОДАТА И ВИСТИНАТА КАКО ИДЕНТИТЕТИ ВО МОДАТА** ....

M.Sc. Anis SEFIDANOSKI, PhD Biljana PERCHINKOVA
NEW MODEL OF ESUPPORT BASED ON MACHINE AUGMENTED INTELLIGENCE...*1285*
M.Sc. Irena SKRCHESKA, M.Sc. Anis SEFIDANOSKI
CLOUD-BASED OPEN INNOVATION PLATFORM *1293*

Assist.Prof.Olivera Gjorgieva-Trajkovska,
University “Goce Delcev”, Shtip,
Faculty of Economics,
Republic of Macedonia
Assist.Prof. Janka Dimitrova,
University “Goce Delcev”, Shtip,
Faculty of Economics,
Republic of Macedonia
Assist.Prof. Aleksandar Kostadinovski,
University “Goce Delcev”, Shtip,
Faculty of Economics,
Republic of Macedonia

THE IMLICATIONS OF GLOBAL FINANCIAL CRISIS ON DVELOPING COUNTRIES-WITH SPECIAL REFERENCE TO MACEDONIA

Abstract

This paper discusses the implications of the global financial crisis for developing countries, with special reference to Republic of Macednia. The crisis, through deleveraging and/or flight to quality, spread to those economies whose companies and banks had no connection with the securities linked to the subprime mortgages that triggered the crisis. The hierarchical and asymmetrical nature of the present international financial and monetary architecture caused these movements to have much greater destabilizing effects on the foreign exchange markets of the emerging-market economies. The global financial and economic crisis has demonstrated the need for major reforms in the system of global economic governance. Such reforms are necessary in order to reduce the predominant influence of financial markets in determining the conditions under which governments design their macroeconomic and development policies. The key to greater stability lie in a multilaterally agreed set of principles and rules for exchange-rate management, accompanied by a framework for macroeconomic policy coordination among the systemically important countries. In developing countries and emerging-market economies the use of capital controls would help stabilize the macroeconomic context for investment in real productive capacity and successful integration into the global economy. Besides the statement of Macedonian government in 2008 that Macedonia will not feel the effects of the global financial crises, based on the fact that Macedonian economy and financial and banking sector waren’t integrated enough in the global one, and its liquidity was based on stable sources, one year after Macedonia has already strongly felt the effects of the global financial and economic crisis, and the country has entered the recession.

The main reason is that Macedonia is a small country and its economy is based on liberal external trade; on the annual level it reaches about 100% and more of the annual GDP of the country.
***Key word:** financial crises, implications, developing countries, Macedonia*

Introduction

The economic crisis that developed in financial markets in the developed world has spread – in a variety of ways – into developing countries. integrated financial sectors, which felt the aftershocks from Wall Street and the City. Next came the impact on trade, as volumes and prices of commodities and manufactures collapsed across the globe. Workers selling food on the street, doing piecework in the home and picking through waste were affected alongside workers in the factories as demand for their services dropped and more people joined their ranks. Remittances from migrant workers in rich countries were also hit, though not as badly as anticipated.

Finally, with an even greater lag time, comes the impact on government spending in poor countries and donor aid budgets – it is yet to be seen whether rich country governments will stand by their aid promises, or force poor countries and people to pay the price of th rich world's financial folly.

Many developing countries enter this crisis with advantages that they lacked during the shocks of the 1980s or 1990s. The strengthening of macroeconomic policies – including fiscal and external positions, in many cases – leaves them less vulnerable.

The first priority is to prevent financial contagion from crippling domestic banking and non-banking financial sectors. Because of the high level of interlinkages among the world's financial firms and sectors, these effects have begun to arrive before the real-economy effects in some countries. Stock markets have declined sharply, some currencies have depreciated substantially, and sovereign interest-rate spreads have risen with the "flight to safety" in world markets. At a more micro level, some developing-country exporters are already finding it hard to obtain the trade credits that are their lifeblood, which could cripple export sectors that will soon be hit by the fall in foreign demand.

Developing countries that enter the crisis with large balance-of-payments and fiscal deficits were the most vulnerable to these effects. Such countries had larger financing and adjustment needs, if the current account swings sharply from deficit to balance as capital dries up, as occurred in the Asian financial crisis. This put a deep strain on the balance sheets of domestic firms and banks, potentially leading to a cascade of bankruptcies and bank failures. If their fiscal resources were already strained to the limit, then it was impossible to mount domestically financed rescues of their financial sectors. These countries were likely had to seek financing for the international financial institutions, especially at a time when bilateral donors are already straining to meet domestic crisis needs.

More generally, developing-country governments have two main macroeconomic tools for responding to the negative shock that is coming their way: monetary policy and fiscal policy. One great risk is that if the credit crisis is not effectively resolved, the global economy could enter a period of deflation like the one that

Japan suffered through in the 1990s. In that environment, standard monetary policy will not likely be effective in the developed economies.

Firms in these countries are already on or near the global technological frontier, so there is limited room for industrial upgrading, meaning that any credit-financed expansion would primarily be in terms of production capacity. But in the face of low demand and excess capacity, developed country firms are not likely to want or be able to borrow to finance expansion.

In the developing world, by contrast, there is more room for credit-financed industrial upgrading, which may give more room for monetary policy to work in those countries that can afford to use it. Not all countries were able to; some found themselves forced to tighten monetary policy and increased interest rates to prevent excessive currency depreciation or capital outflows.

On the fiscal-policy side, developing-country governments have a variety of tools that they could use to cushion the blow of the shock. Governments with some fiscal space can respond by injecting some well-designed fiscal stimulus into their economies, to generate domestic demand that can offset the expected decline in foreign demand. Developing countries have pressing needs that can be met through public investments. One such need is building of infrastructure, especially after a period when private-sector growth has sometimes outstripped the ability of the public sector to provide the infrastructure needed to sustain that growth and rural infrastructure where the infrastructural gap exists between urban and rural areas.

A brief outline of the crisis

The origins of the current world financial crisis are now well known. They lie in the worldwide financial excesses of the past few years and even decades; the bursting of the housing and oil price bubbles; excessively low interest rate policies; massive trade surpluses in some countries and trade deficits in others; and savings rates that are too low in some parts of the global economy and too high elsewhere.[1] The cumulative effect is a financial and liquidity crisis that become a global macroeconomic upheaval, with significantly negative world GDP growth, sharply increased unemployment, pressures on public revenues and deflation.

In developed countries, the crisis stems from a drying up of credit flows as financial institutions are no longer able to assess the creditworthiness of other enterprises, whether financial or nonfinancial. For instance, the inability of some companies to obtain insurance for orders they have placed with suppliers has caused them to curtail or shut down their production and sales activities. This problem has been aggravated by developments on the demand side, with households compelled to increase their savings to compensate for the fall in the value of their financial and real estate assets. Rising fears of unemployment have also led households to curtail consumption. In this sense, the crisis differs from most of those in the past in that the problem is not a lack of demand for credit but a lack of supply of credit.

For the developing countries, which have become increasingly integrated into global trade and finance over the past few decades, the crisis is not one of credit but of falling demand in the markets of developed countries. The financial crisis in the developed countries did not initially affect developing and transition

[1] Marcelo de Paiva Abreu, The Effect of the World Financial Crisis on Developing Countries:An Initial Assessment, 2009

economies as the crisis did not originate within their financial systems. It was even hoped that the real economy in the developing countries would escape unscathed and even that growth in developing countries would help to buoy the world economy, as it did in the recession at the beginning of this century. But when demand fell in developed countries, volumes and prices of exports from developing countries declined. This initial severe contraction of output and employment in the export industries of developing and transition countries in turn has spread to other industries in these countries, causing economy-wide declines in output and employment.

The extent of the effects of the global crisis on developing countries depends on the importance of exports and capital inflows in their economies. Countries that depend on exports of primary commodities other than oil have also been hit hard because of the sharp decline in prices of export commodities.

The increasing integration of world finance also means that the crisis is having a serious effect, both directly and indirectly, on investment in developing countries. Not only is foreign direct investment (FDI) declining, but foreign financial institutions are withdrawing their investments in developing countries' stock exchanges and repatriating the proceeds, resulting in sharp declines, often of more than 50 percent, in stock prices and large devaluations, often of more than 25 percent, in their currencies. The drop in stock prices further hurts investment in developing countries; the effect of currency devaluation, however, depends on the share of imported inputs in production or in the consumption basket of workers.

The financial crisis had its immediate reverberations in those developing countries that were closely linked to the global financial markets, as capital took refuge in safe havens and there was a rapid flight of capital from emerging markets to the advanced economies and particularly the US. This initial impact on the developing countries , however, was less pronounced as they were less integrated into the global fi nancial markets. With the
deepening of the financial crisis, freezing of credit, and the sharp fall in the market value of private wealth, the financial crisis turned into a crisis of the real economy, beginning in the fall of 2008. The least developed countries have been affected more during this later phase of real economic crisis.

The global economic crisis has led to a sharp reduction in world trade and rapid decline in commodity prices. Th is is one of the main mechanisms through which developing countries have been affected.

Foreign direct investment (FDI) flows which achieved their highest level in 2007 have been declining rapidly since the onset of the financial crisis. The decline in FDI is the second channel through which the developing economies have been aff ected.

A third transmission mechanism, which can be of critical importance for some developing and least developed countries, is the slowdown in migrant workers remittance flows. As unemployment in the advanced countries increases and the end of the commodity export boom in some of the labour importing developing countries reduces the demand for migrant labour, the labour exporting developing countries have experienced noticeable declines in remittance flows.

The economic crisis has led to a sharp deterioration in the fiscal position of all advanced economies. This put pressure on the Official Development Assistance (ODA) budget of the Organisation for Economic Cooperation and Development (OECD) countries, which had dire consequences for the developing

countries.The impact of the global economic crisis on the developing countries is thus multifaceted, and affected different countries in different ways, depending on the mode of integration of the particular country in the global economy and the structure of its domestic economy.

Besides the great deal of uncertainty with regard to the depth and length of the economic recession in the advanced countries, it is nevertheless clear that the global crisis had important implications for growth and poverty in the less developed countries and for the achievement of the Millennium Development Goals. This can be particularly onerous, as the current global crisis has arrived on the heels of the food and fuel crisis of 2007 2008 which inflicted a great deal of hardship on non-oil exporting countries.

The global financial crisis have caused a considerable slowdown in most developed countries. Governments around the word tried to contain the crisis. Stock markets were down more than 40% from their recent highs.[2] Investment banks have collapsed, rescue packages were drawn up involving more than a trillion US dollars, and interest rates have been cut around the world in what looks like a coordinated response. Leading indicators of global economic activity, such as shipping rates, were declining at alarming rates.

Impact of the financial crisis on developing countries and their response

The financial crisis affected developing countries in two possible ways. First, there was financial contagion and spillovers for stock markets in emerging markets. The Russian stock market had to stop trading twice; the India stock market dropped by 8% in one day at the same time as stock markets in the USA and Brazil plunged. Stock markets across the world – developed and developing – have all dropped substantially since May 2008. We have seen share prices tumble between 12 and 19% in the USA, UK and Japan in just one week, while the MSCI emerging market index fell 23%. This includes stock markets in Brazil, South Africa, India and China. We need to better understand the nature of the financial linkages, how they occur (as they do appear to occur) and whether anything can be done to minimise contagion.

Second, the economic downturn in developed countries had also significant impact on developing countries. The channels of impact on developing countries include:

• **Trade and trade prices**. Growth in China and India has increased imports and pushed up the demand for copper, oil and other natural resources, which has led to greater exports and higher prices, including from African countries. Growth in China and India was likely to slow down, which had knock on effects on other poorer countries.

• **Remittances.** Remittances to developing countries declined. There were fewer economic migrants coming to developed countries when they are in a recession, so fewer remittances and also probably lower volumes of remittances per migrant.

• **Foreign direct investment** (FDI) and equity investment. These was under pressure. While 2007 was a record year for FDI to developing countries, equity finance was under pressure and corporate and project finance were already weakening

[2] Overseas Development institute: *The global financial crisis and developing countries*. October, 2008.

• **Commercial lending**. Banks under pressure in developed countries were not able to lend as much as they have done in the past. Investors were, increasingly, factoring in the risk of some emerging market countries defaulting on their debt, following the financial collapse of Iceland. This limited investment in such countries as Argentina, Iceland, Pakistan and Ukraine.

• **Aid.** Aid budgets were under pressure because of debt problems and weak fiscal positions, e.g. in the UK and other European countries and in the USA.

• **Other official flows**. Capital adequacy ratios of development finance institutions were under pressure. However these have been relatively high recently, so there is scope for taking on more risks.

Each of these channels needed to be monitored, as changes in these variables had direct consequences for growth and development. Those countries that have done well by participating in the global economy lost out most, depending on policy responses, and this was not the time to reject globalisation, but to better understand how to regulate and manage the globalisation processes for the benefit of developing countries. The impact on developing countries varied. It have depended on the response in developed countries to the financial crisis and the slowdown, and the economic characteristics and policy responses, in developing countries.

Given the fact that there has been a worldwide trend towards external opening in recent decades, the global crisis had severe effects on developing countries. As indicated, remittances showed some resilience. Financial turmoil had stronger effects on middle income countries more integrated into world financial markets, whereas low-income countries dependent on official flows have remained less affected by the capital flows channel. Given the magnitude of the collapse of commodity prices, the trade channel affected all countries, but was likely to affect commodity-dependent economies more, many of which are low income countries. Countries with stabilization funds (generally, energy exporters and some metal exporters) were able to use past savings to cushion the effect of commodity price downswings.

National responses aimed to mitigate the contractionary effects coming from abroad and to rethink their trade strategies. The room for maneuver to adopt expansionary fiscal and monetary policies depended on balance of payments constraints. In the case of fiscal policy, it also depended on recent fiscal stances, inherited public sector debts and the existence (or the absence) of well-developed domestic bond markets where the public sector could finance its current imbalances in non-inflationary ways. Given the dependence on balance of payments constraints, the availability of external financing was critical.

The dominant pattern over this period was an increasing number of countries with current account (and indeed larger size) deficits. This trend was matched, however, by broad-based and, in many cases, large improvements in debt ratios and, to a lesser extent, by foreign exchange reserve accumulation. Debt improvements were associated both with domestic policies and with the major debt relief initiatives for low-income countries (the Multilateral Debt Relief Initiative and a major debt relief granted individually by the Paris Club). [3]

The nature of the policy packages that were adopted depended on the countries' current stance. For those countries with a strong debt and foreign exchange reserve position but relatively weak fiscal stance, the

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[3] Working paper: *The financial crisis and its impact on developing countries*. UNDP, 2009

room for maneuver lied more in monetary than with fiscal policy. More generally, most emerging economies had the capacity to avoid the traditional pro-cyclical monetary policies of past crises and followed the expansionary policy trajectories of industrial economies. Most had actually adopted policies to ease domestic financing, to facilitate access of private sector companies to foreign exchange and, to a lesser extent, to reduce domestic interest rates. They should continue to move in that direction. A similar rule of easing monetary policy should be followed by other developing countries.

In the fiscal area, there was significant room to maneuver in a relatively large group of developing countries. They used this space to mitigate the effects of the external shock. Infrastructure investment and social spending were in the focus of these programs. The strategy depended on each country's social policy framework. Universal social policies in the areas of nutrition, basic education and health should be the major policy focus, but targeted programs for the poor, such as conditional cash transfers, make sense in middle-income countries (in poorer countries, by definition, poverty is widespread and universal programs are clearly superior). Special emergency employment programs were also the essential complement, since unemployment insurance, the traditional automatic stabilizer of industrial countries is generally absent in developing countries. Within the available mix of policies, experience indicates that tax reduction policies are unlikely to have the best effects and, rather, strengthening the tax base should be the focus of policy makers.

Although trade opportunities are not generally viable, trade policy also played a important role in the recovery in at least three different ways. First, non-traditional exports could be encouraged, particularly in commodity-dependent economies, through a mix of exchange rate depreciation and sectoral incentives. Second, the possibility of strengthening domestic linkages of existing manufacturing export activities could also play a role. Third, more active South-South cooperation could play a role, by encouraging trade through existing integration processes. Payments agreements among central banks also plaedy a role in facilitating such trade without the need for hard currencies.

Finally, and very importantly, the crisis provided an opportunity to rethink the role of domestic markets, which were largely left out from the radar of policy makers during the reform period. Indeed, a major implication of expansionary macroeconomic policies was that all countries can contribute to the global economic recovery by focusing on their domestic demand. Protection policies would be clearly counter-productive, generating beggar-thy-neighbor effects. But policies that focus on the mass market for consumer goods and on strengthening small- and medium-sized enterprises, which tend to depend heavily on local markets, can play a role in policy packages that place domestic demand again at the center of economic policy.

The impact of the global financial crisis on Macedonian economy

Towards the middle of 2008th, when the global financial crisis was hanging with all its strength, the Macedonian Government thought that Macedonia will not feel the effects of the global financial crisis. It even stated in certain occasions that the Macedonian economy will make profit out of the crises. This statement has been supported with the fact that The Macedonian Financial and Banking Sector wasn't integrated enough in

the global one, and its liquidity was based on stable sources (deposits of the citizens and cooperative sector), so significant disrupt in the Macedonian economy couldn't occur.

One year after this "Don't worry" policy, Macedonia has already strongly felt the effects of the global financial and economic crisis, and the country has entered the recession. According to the official preliminary data from the State Statistical Office, Macedonia's GDP in the first two quarters notes decreases of 0,9 % and 1,4 %.[4]

Macedonia is small country and its economy is based on liberal external trade; on the annual level it reaches about 100% and more of the annual GDP of the country. The economy depends on the import of goods, which is nearly twice bigger than the export of the country. As a result of that, Macedonian trade deficit reached the level of over 25% of the GDP in 2008 with absolute value of over 2, 5 million dollars.

Traditionally, in significant part, the high trade deficit has been financed from the money transfers of Macedonian workers abroad. The global crisis has affected these transfers despite the fact that the growth of the trade deficit has remained on the same level. These disadvantages have created huge deficit on the current account, of 14% of the GDP in 2008. Thus, Macedonia has entered the state of economic recession, followed by a strong decline of the situation in the external sector.

The global financial and economic crisis that erupted in 2007 and 2008 and the ensuing Great Recession had a huge impact on the Macedonian economy. Previous healthy growth rates were rapidly interrupted towards the end of 2008, and GDP even fell in 2009, before recovering sluggishly in 2010-2011 and then slightly falling again in 2012.

As a small open economy, heavily dependent on trade and financial links with other countries, it is commonly thought that the trade channel was the strongest transmission channel. Indeed, exports were the first to react to the crisis, falling rapidly by 6.3 % in 2008 and 15.8 % in 2009, in real terms.[5] Other GDP components were more sluggish, but eventually they also adjusted downwards. Imports only slowed down in 2008, but then fell by 14.3% in real terms in 2009. Most of the adjustment in domestic demand also occurred with some delay,

with personal consumption falling by 4.7% in 2009, while gross investments were almost unchanged in 2009 and then fell by 6.7% in 2010. However, the effects of the crisis were also felt via the financial channel. Unlike most other countries, this was not so much due to the halt of foreign funding, as lending was mostly financed by domestic deposits, but to the heightened uncertainty and consequently the more conservative bank lending activity.

Indeed, credit growth slowed from 34.4% in 2008 to 3.5% and 7.1% in the end of 2009 and 2010 respectively, and is still far from the double – digit growth before the crisis. In addition, the uncertainty regarding the euro crisis also affected private transfers, which are essential in financing relatively large trade deficits. Their annual growth became negative in the final quarter of 2007, and they continued to fall in most of 2008 and early 2009.

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[4] Friedrich-Ebert-Stiftung, Office Macedonia: *The Impact of the Global Financial Crisis on the Macedonian Economy and the Economic Situation in the Macedonian Households*, October, 2009

[5] Rilind Kabashi: Effects of the global crisis on Macedonia: a counterfactual analysis.academia.edu

Finally, these movements in the economy, and particularly in foreign reserves, resulted in various policy responses by the central bank. Unlike most other central banks, the NBRM was tightening its policy until March 2009 in order to maintain the exchange rate stability, and then kept it unchanged by the end of 2009 before the start of its gradual relaxation. In addition, the central bank intervened in the market by selling foreign currency, particularly in the first half of 2009. The central bank also undertook additional measures in order to maintain and strengthen financial stability. Certainly, monetary policy actions were significantly affected by the need to maintain a stable exchange rate, while inflation slowed down due to supply side factors, which implied that output
movements had only secondary priority in the early stage of the crisis. However, once foreign reserve movements were stabilised, the central bank did pay additional attention to supporting economic growth.

The banking system has retained the role of the most developed financial sector in the Macedonian economy. Total assets of the banking sector on 31.12. grew by 7.1%, in comparison from last year. The reasons for the dominant role of the banks were:[6]

- The traditional role of the banks as major financiers of the Republic of Macedonia,
- Poor development of the financial markets,
- Deregulation and competition in the banking sector,
- High profitability of banks.

The global financial and economic crisis, had a different impact on the Macedonian financial and real sector. The Macedonian financial and banking sector was not directly affected by the global financial crisis, but could not avoid the negative effects of the global recession movements, that were spilled on the domestic real sector, and through reduced production and consumption on the banking sector, as well. The stable position of the banking sector was result due to its closeness to international financial markets, lack of exposure to "toxic financial products," its strong capital and liquid position, caution in taking risks, and effective prudential measures taken by the National Bank of Macedonia (NBRM). Although the world crisis has been spread on the relation: financial - real sector, in Republic of Macedonia, an opposite case had happened, so the crisis occurred, because of the recession, that limited and reduced the lending and financing, afterwards.

The first attack by the crisis in 2009, has created great pressure on the Macedonian denar, because of the high euroisation of the financial obligations in the country, where has emerged some serious pressures and risks on the financial stability, which can be seen, through increased buying of euros, reduced volume of capital flows and the existence of an imbalance of foreign exchange market, which created some conditions devaluation rate. This situation waseven greater, if we known to the Macedonian denar is pegged to the euro and the trade deficit is very high and the reserves are limited.

Solutions for overcoming the consequences of the crisis in Macedonia

[6] Marijan Stevanovski, Aleksandar Dejanovski*: The Consequences of the World Economic Crisis on the Macedonian Financial and Real Estate Sector*. TEM Journal – Volume 2 / Number 1/ 2013

Having in mind the mentioned effects the global economic crisis had on the macedonian economy, the primary challenges facing economic policy decision makers were:

- how to alleviate the effects of the crisis without disrupting market principles, while at the same time helping with long term measures that will improve the competitiveness of the domestic economy, and
- how to finance the domestic economy, in circumstances of reduced domestic demand and reduced economic activity as a result of reduced external consumption.

The approach which promises the most appropriate solutions was a cooperation between economic policy decision makers, experts and the business community. Based on the already established dialogue with the business community, from the end of 2008 up to the third quarter of 2009 three packages of so called anti-crisis measures have been implemented.[7]

The first package of anti-crisis measures (November 2008) was comprised of 10 measures aimed at relieving the economy, valued at 300 million euros. These measures were directed at improving the liquidity of companies by eliminating certain income taxes (companies do not pay income tax if they do not distribute it to the owners of the companies, which means this money remains as operational funds for the companies); the writing off of interest payments due to unpaid personal income tax, income tax and real estate tax; payments for pension insurance of the most vulnerable categories of labor intensive companies; reprogramming of tax obligations, more precisely those companies that are experiencing difficulties in their work were able to pay their tax in installments up to three years. Furthermore, among the first package of anti-crisis measures are also measures that were implemented at the request of companies-customs breaks for importing equipment, raw materials and repro-material intended for production. This lifted customs for approximately 500 tariff items.

The second package of anti-crisis measures (March 2009) promoted an investment program with infrastructure projects in energy, transport, environmental protection, education and culture. Total investments amount to 8 Billion Euros which were planned to be realized over the next 6--8 years with state investments, private investments or public-private partnerships. The goal was to more easily overcome the global crisis in the coming period and to continue the investment cycle, and with that to alleviate the effects of reduced foreign demand on the domestic economy.

The third package of anti-crisis measures (May 2009) encompasses 70 measures refered to three segments: first - the rebalancing of the 2009 budget; second - credit support for companies; and third - other measures aimed at reducing barriers and costs of doing business by companies.

The rebalancing of the 2009 budget was aimed at reducing expenditures in order to adapt to reduced income, which was supposed to save money that sould be used to maintain the macro-economic stability of the country and maintain a stable exchange rate for the denar. The need for a rebalance was because of the creation of a fiscal policy, which through increased productive investments, which also included public investments,

[7] Dr. Fatmir Besimi, Minister of the Economy of the Republic of Macedonia: The global economic crisis and the challenges facing the Republic of Macedonia.2009

was aimed at efficiently stimulating the expected slowing of economic activity caused by the crisis.
As far as credit support for companies is concerned, a package of measures for direct credit support of the private sector was adopted, through a credit line from the European Investment Bank (100 million euros). The money were earmarked for support of small and medium size companies, which employ the largest percentage of workers in the Republic of Macedonia (approximately 90% of all employed in industry). The support was realized through the Macedonian bank for development promotion (100 million euros) and the commercial banks (100 million euro). Macedonian bank for development promotion participated with subventions for interest payments for small and medium size companies (interest rates were approximately 6%, which was less than the current market interest rate of 12%), and in subventions for the guarantees that the commercial banks are asking from companies for extending credit lines to them, as well as for extending guarantees from the Macedonian bank for development promotion for Macedonian companies trying to enter foreign markets.

The other measures for supporting companies, through a reduction of barriers and costs of doing business in the Republic of Macedonia are part of a mosaic of greater measures. More precisely, this package of measures refered to measures to simplify customs procedures and speed up the flow of goods through the border. The successful implementation of the first phase of the project Regulatory guillotine contributed to a reduction of bureaucracy, expenses that companies make to receive permits, confirmations, approvals and other administrative services, which burden every day work.

Besides the three packages of anti-crisis measures, aimed at securing greater macro-economic stability, sustaining domestic financial liquidity and stability of the exchange rates in circumstances in which trade deficits have increased and reduced FDI's,the need appeared for additional external financing of the domestic economy in order to compensate for reduced foreign demand. This was especially important for macedonian macro-economic stability, especially because of the policy of the monetary authorities to maintain a stable exchange rate, when foreign financing will directly influence the reduction of interest rates and increase foreign currency reserves. Having these arguments in mind, the Republic of Macedonia issued euro-bonds in the amount of 175 million euros.

Macro-economic movements in the first three quarters of 2009 indicated that macro-economic stability have been maintained, in the sense of stable prices and a stable exchange rate, which for a small and open economy is of exceptional importance in creating a favorable business climate. In the long run this created conditions to attract more investments, which with new technology and know-how can make the domestic economy more competitive on the world markets.

Along with the continuing dialogue with the business community and the monitoring of current economic movements, further measures had been prepared, like a new rebalancing of the Budget, new reductions and elimination of customs for repro-material and equipment for production, as well as other forms of support for companies based on market principles and the functioning of an open economy.

Despite the challenges Macedonian economy was and is still facing due to the effects of the global economic crisis, it still have to solve the chronic transition problems, more precisely the several year long trade

deficit and unemployment. At the same time the main challenge remains –h ow to increase the competitiveness of the domestic economy, so that it can handle global competition, which is especially important for a small and open economy. The goals of macedonian economic, industrial and trade policy is to create a horizontal frame (according to the Lisbon convention), which has to link the constant improvement of the business climate, attract investments and increase innovation in science. This will influence the creation of a new structure of import and export, constant economic growth and improve the living standard.

Conclusion

The financial crisis had its immediate reverberations in those developing countries that were closely linked to the global financial markets, as capital took refuge in safe havens and there was a rapid flight of capital from emerging markets to the advanced economies and particularly the US. This initial impact on the less developed countries, however, was less pronounced as they were less integrated into the global fi nancial markets. With the deepening of the financial crisis, freezing of credit, and the sharp fall in the market value of private wealth, the financial crisis turned into a crisis of the real economy, beginning in the fall of 2008. The lessdeveloped countries have been affected more during this later phase of real economic crisis. The global economic crisis has led to a sharp reduction in world trade and rapid decline in commodity prices. This is one of the main mechanisms through which these countries have been affected.

In the Republic of Macedonia, as a small and open economy, the effects of the global economic crisis were felt with a certain delay. The impact was primarily in the real sector, through the foreign trade exchange, as a consequence of which there was a drop in industrial production, an increased trade deficit and reduced FDI's. This in turn reflected itself in reduced budget income, reduced financial liquidity and increased interest rates.

Eliminating certain taxes, reducing customs for repro-material and machines, the investment program in infrastructure, the rebalancing of the budget, foreign credit lines (in order not to reduce domestic demand), as well as the securing of funding for the Macedonian bank for development promotion in order to secure cheaper credits for small and medium sized companies, were part of the measures which we undertook to alleviate the consequences of the crisis. At the same time, attention was paid to make sure that the measures would have an effect in reducing the consequences of the crisis, but at the same time that they are market oriented so that in the long run they will increase the competitiveness of the domestic economy.

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