

## Editor's Note

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This ninth volume of the *Croatian Economic Survey* comprises a selection of articles originally published in *Privredna kretanja i ekonomska politika* journal (Economic Trends and Economic Policy) in 2006. The selected articles were originally published in Croatian and by collecting them in this volume I hope they will reach a broader international audience. One of the aspirations of this volume is to intensify the discussion of Croatian economic issues. At the same time, the authors will hopefully receive a response to their work, which could be inspiring for their future research.

Five articles have been selected for this volume. They cover empirical as well as policy-oriented contributions in rather diverse topics. All the selected papers deal with the issues which are widely discussed in Croatia and brought into the focus of scientists, and a wider public as well. The papers are presented in chronological order.

Even though the regional policy is in place in Croatia, its subject matter has not been clearly defined. The first paper “Uncovering Regional Disparities – the Use of Factor and Cluster Analysis” by *Ivana Rašić Bakarić* addresses the issue of lacking methods and data for formulating a sound regional policy. It presents a possibility of using the factor and cluster analysis as a tool for the classification of spatial-economic units in order to support a regional development policy. Classification is based on eleven economic and social indicators. Local government units of the County of Istria, the Lika-Senj County and the Primorje-Gorski Kotar County are used as a working sample. Factor analysis helps to identify a small number of socio-economic dimensions that adequately summarise the information contained in the original set of variables, while the cluster analysis is used to look for groups of towns and municipalities with similar levels of socio-economic development. Multivariate techniques were successful in identifying the main axes of socio-economic characterisation and the regions of the observed counties with differing degrees of development. This methodology for spatial-economic entities' classification enables a much more useful characterisation of the territory for policy-making purposes. Regional policy measures can lead to desired and equal effects in a specific region only if implemented in territorial entities that are homogenous in regard to dimensions of social and economic development.



The second paper, prepared by *Jelena Budak*, elaborates on the issue of corruption in Croatia. Specifically, the article “Corruption in Croatia: Perceptions Rise, Problems Remain” presents the main hypothesis that there is a high perception of corruption in Croatia, which is an obstacle to socio-economic development. Fighting corruption is a necessary criterion for the Croatian membership in the European Union, and a lack of the effective implementation of anti-corruption policy measures makes the existing anti-corruption policy still inefficient. The author analyses corruption prevalence in Croatia from three different viewpoints. Firstly, she examines the international ranking of Croatia as a relatively highly corrupt country. This is followed by an analysis of recent survey results investigating the corruption perceptions of citizens. Finally, the corruption perceptions of entrepreneurs in Croatia are considered. The results point out sectors and forms of highest corruption prevalence. The importance of corruption as an obstacle to the development of entrepreneurship is also evaluated. The comparison of the adopted anti-corruption measures with the EU recommendations indicates that the implementation requires further and continuing efforts, with political commitment being the essential factor. The anti-corruption policy recommendations emphasise the importance of fighting corruption for the general benefit of Croatia, and not only in the context of the future membership in the European Union.

The third article “Maastricht Criteria and the Inclusion of Underground Economy – the Case of Croatia” by *Željko Lovrinčević*, *Davor Mikulić* and *Zdravko Marić* discusses the consequences of underground economy by comparing basic macroeconomic data on Croatia and the new EU member states. European Union has introduced an explicit obligation for all member states that the official GDP data need to include an estimation of underground economy, resulting from statistical or economic reasons. For this purpose, the so-called Eurostat Exhaustiveness programme has been developed for the group of candidate countries, ten of which have become full members as of the 1st of May 2004. In line with the results of this programme, the new EU members include the correction for the value of underground economy into their official GDP figure. The authors show that with the inclusion of underground economy, the consequent value of Croatian per capita GDP, measured according to the purchasing power parity, reduces the gap in comparison to the EU-25. Furthermore, the proportion of total expenditures in GDP of the general government sector is reduced as well, which places Croatia below the NMS-8 country average. In terms of the Maastricht convergence criteria, the underground economy inclusion procedure does not affect the fact that the criteria are not met.



The article stresses out that the inclusion of underground economy influences two indicators: proportion of the government sector deficit in GDP and the proportion of the public debt in GDP. The inclusion of underground economy does not have any influence on fulfilling the criteria concerning the government sector deficit. The criteria concerning the size of public debt are fulfilled by Croatia even without the inclusion of underground economy. The authors find that the inflation criteria and the size of long-term interest rates criteria are not directly linked to the GDP value.

In her article “The Effects of Market Orientation on Product Innovation” *Ljiljana Božić* discusses the influence of market orientation components on the introduction of product innovation with a different degree of novelty in Croatian companies. Bearing in mind that different kinds of product innovation may contribute to business performance in different ways, the importance of market orientation for business performance may indirectly be explained by the influence of market orientation components on the introduction of a product with a specific degree of novelty. However, the focus of this paper is put exclusively on the relationship between market orientation and innovation, and the author does not want to suggest that any type of product innovation is superior in respect to its contribution to the overall business performance. It is argued that giving preference to any type of product innovation does not necessarily lead to a superior business performance. Just introducing an imitation of a competing product with some slight modifications can hardly lead to an extraordinary advantage over competitors and high profit. On the other hand, focusing only on the development of exclusively discontinuous innovations would hardly lead to a high profit. Such a focus would actually lead to the creation of products that competitors would imitate and realise the highest benefits with a minimal investment at the moment when accepted by consumers.

The last paper “Structural Changes in Tertiary Education and Impacts on the Labour Market” by *Zdenko Babić*, *Teo Matković* and *Vedran Šošić* analyses the dynamics of the labour market and the Croatian tertiary education system. As Croatia has embraced an idea of the knowledge based economy, the quality of tertiary education system gains in importance, at the same time challenging the authors to point out key organizational problems within the tertiary education system and offer some possible recommendations for improvements. Like graduates in many other countries, Croatian university and college graduates have better jobs with higher wages, higher activity rates, longer careers, lower unemployment rates and better employment prospects. Even though the total

student population in Croatia rose by 82 percent between 1990 and 2005, this expansion was dominantly concentrated in the field of social sciences and humanities, in non-university courses and among students who (partly) pay tuition fees. At the same time, the number of students whose education fees are fully covered by public sources has decreased. The authors find that the educational infrastructure has not kept pace with this increasing trend, while the proportion of private fees in the total tertiary education cost has exceeded 20 percent in the 2000s. By using aggregate data on employability of university graduates the authors observe the extent to which publicly financed university entry quotas have followed the changes in labour market demand. By comparing data on recent university graduates from programmes with low and high employability, the authors find that publicly financed entry quotas for different faculties were for the most part not in congruence with trends and demands in the labour market, but they were largely the result of a revenue maximization and capacity utilisation strategy, followed mostly by college boards (mainly in the social sciences and humanities), thus creating some disproportion in the highly-educated segment of the Croatian labour market.

I hope this note will provoke your interest to focus more deeply into the selected articles and that the offered diversity of topics as well as the quality and clarity of their presentation will satisfy your professional and intellectual curiosity.

Guest Editor:

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