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CHALLENGES OF TOURISM AND BUSINESS LOGISTICS IN THE 21ST CENTURY



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For the Publisher:

Nikola V. Dimitrov, Ph.D. – Dean

Edited by:

Nikola V. Dimitrov, Faculty of Tourism and Business Logistics, "Goce Delčev" University - Štip, *Macedonia*
Drago Cvijanović, Faculty of Hotel management and Tourism in Vrnjačka Banja, University of Kragujevac, *Serbia*
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Natasа Miteva, Faculty of Tourism and Business Logistics, Goce Delcev University - Štip, Macedonia

Proofreader:

Marija Krsteva, Faculty of Philology, Goce Delcev University - Štip, Macedonia

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PREFACE

The Faculty of Tourism and Business Logistics in Gevgelija, at the Goce Delcev University - Stip, hosted the First International Scientific Conference, "Challenges of Tourism and Business Logistics in the 21st Century".

The conference was held on 24 and 25 October 2017 in Gevgelija with an optional visit to Dojran - Dojran Lake.

32 works of 60 authors from Serbia, Latvia, Turkey, Poland, Bulgaria, Kosovo and Macedonia were presented at the Conference.

The purpose of the Conference is exchange of ideas and experiences of the participants coming from Macedonia and abroad, and establishment of cooperation for further development of tourism and business logistics in Macedonia and beyond.

The results of the Conference are visible through publication in a collection of papers, which is presented to a wider scientific audience and the public.

In this way, we want to promote the Faculty of Tourism and Business Logistics, to promote Gevgelija and Dojran as the most visited settlements in the south-eastern part of Macedonia.

Gevgelija - Stip,
December 2017

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Nikola V. Dimitrov Ph.D. *Dean*

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ADDRESSING DE-EUROIZATION IN TRANSITION ECONOMIES: THE EVIDENCE OF MACEDONIA

Tatjana Boshkov¹

Abstract

Considering the exchange rate experience of Macedonia, it's likely to remain significantly euroized country for an extended period. IMF considers that the appropriate strategy is the one which provides support for the gradual de-euroization for maintaining macro-prudential policy, development of the domestic market and maintain prudent policies that mitigate the risks of foreign currency. The investigation indicates that macroprudential policies are becoming an important driver of de-euroization. In terms of other drivers of euroization the findings of this analysis support the conventional view that deposit euroization and the interest rate differentials were the main determinants of credit euroization in Macedonia. Also, this paper analyzes the main reasons for the process of euroization in Macedonia and will be presented any aspect of the potential benefits of de-euroization.

Key Words: *euroization, de-euroization, foreign currency, economy, growth.*

1. Introduction

Euroization is a problem with a long history and usually persistent phenomena. The high level of euroization is common in emerging countries in Europe as in countries with fixed exchange rate regime.

In the countries in Western Balkans has been identified a strong presence of foreign currency.

The fact is that transactions could take a place outside of the banking channels, which is not a case for Fx-loan and Fx-deposit ratios because there is no the whole scale of euroization. How much foreign money are in the economy is difficult to measure. This the reason to use data for currency substitution index. This index is high for Macedonia which

¹ Tatjana Boshkov, PhD, Ass. Professor at Faculty of Tourism and Business Logistics, University "Goce Delcev", Stip, Macedonia, e-mail: tatjana.boshkov@gmail.com; tatjana.boskov@ugd.edu.mk

indicate high level of real euroization. After the crisis, the levels are reduced (lower remittances from abroad).

Considering the exchange rate experience of Macedonia, it's likely to remain significantly euroized country for an extended period. IMF considers that the appropriate strategy is the one which provides support for the gradual de-euroization for maintaining macro-prudential policy, development of the domestic market and maintain prudent policies that mitigate the risks of foreign currency. This paper shows the persistence of FX mainly in Macedonian economy and discusses for the benefits and costs, in light of the recent economic crisis.

2. Characteristics of Euroization identified in the literature

Proponents of euroization point a number of advantages that it brings in the form of reduced interest rates, increased currency stability because of low inflation, reduced transaction costs and volatility in exchange rates, thus stimulating foreign trade and facilitating the implementation of structural reforms.

a) Decline in interest rates

By euroization is expected decline of interest rate, flattening of high interest rates with international interest rates and the interest rates of the European Monetary Union.

Also, there are expectations to stabilize short-term interest rate, which will be defined by the monetary policy of ECB and stabilization of exchange rate, too. This means that, the imbalance between aggregate supply and demand will be eliminated through the profit and the prices. In the long run, euroization has no effect on long-term interest rates, because they are determined by savings, investment, risk of outstanding debts and so on. If in the country there is no flexibility in wages and prices, the short-term effect of reducing the risk of foreign exchange rate would result in increasing the cost of borrowing, and thus an increase in the risk of non-realization of cash obligations (Bishev and Boshkov, 2015).

b) Reduction of transaction costs and elimination of exchange rate volatility

Another expected advantage of unilateral euroization is the elimination of exchange rate volatility and reduced transaction costs from the currency exchange, which creates opportunities for increasing the international trade and economic growth. The reduction of transaction costs and the elimination of foreign exchange risk contribute to increase the economic integration with euroized countries, i.e. EMU, since all transactions are exempt from exchange rate risk.

c) Reducing the inflation rate

In some way, euroization can be considered as anti-inflatory strategy. Regardless of the money supply and exchange rate policies which are no longer under the authority of the national central bank, all empirical studies show that application of full euroization makes a decline in inflation rate. In the short-term due to the equalization of prices can lead to

inflation growth, and in the long run will come to an equalization of inflation between euroized countries and countries whose currencies are used.

If the economy is adjusted to a certain level of inflation, the reduction of the real money supply will have an adverse effects on the rate of economic growth and employment, and increasing the monetary stability will improve economic conditions and will make the country more attractive to foreign investors (Boshkov, 2015). Also, there will be no equivalence between all prices due to controlling the prices, so in the long run can be determined the effects of euroization. Also, euroization represents a trade-off solution for alternative exchange rate regime. If the country accepts unilateral euroization, monetary policy regime becomes exogenous factor on which national political public has no impact, which in turn, prevents any political controversy with elections.

Despite the advantages, euroization has its negative consequences which are evident in unforeseen costs and risks.

a) Costs of euroization

The biggest costs of euroization are losing the seigniorage and the role of the central bank as lender of last resort. The seigniorage (Segniorage) is the difference between the nominal value of money and the cost of their production. As possible compensation for loss of money emission profits may be the division of emission profit of country whose currency is used. The appearance of the euro and the international competition among the three major world currency bloc may affect the future on increasing the preparedness of the countries in sharing emission profits. Maastricht Treaty defines the seigniorage revenues to be divided between the Member States (but not for the countries that have accepted the euro on a unilateral basis). Next cost of unilateral adoption of the euro, is the loss of foreign exchange reserves that must be spent to pull the domestic currency. If the hyperinflation devaluates the national currency, than the cost of lossing foreign exchange reserves are small (Bishev and Boshkov, 2015).

Although the biggest cost of euroization is the loss of seigniorage, it should not overlook the fact that the seigniorage can be negative. One reason for the negative seigniorage lies in the depreciation of the domestic currency. Another factor that can lead to reduced emission income is the change in the exchange rates of international currencies in which national reserves are held. For example, if the euro appreciated, the domestic currency will depreciate and emission gain can be negative.

b) The role of the central bank as lender of last resort

With the unilateral introduction of the euro, the central bank loses the function lender of last resort. In economic terms, the function of a central bank as lender of last resort means approval of emergency loans for liquidity of the bank in crisis conditions, which have a degree of urgency and without them it can occur problems that could threaten the target bank system. The role of the lender of last resort, was much more difficult with logistical problems, because of performing a number of key services and the execution of payments in large amounts, the country was forced to rely solely on private arrangements with credit institutions.

In the absence of central bank as lender of last resort, the solution would be:

- domestic banking system owned by foreign banks, which would provide the necessary funds if the bank falls into illiquid condition;
- the remaining reserves after euroization are exploited for establishing special funds responsible for solving crisis situations and bridging the problem of insolvency of the bank;
- increase the requirements for liquidity, efficiency and supervision in the banking sector in accordance with international standards.

c) Costs related to currency stability

Although as an exceptional and primary objective of central banks in developed countries indicate the price stability, the initial positive effects of euroization that can be seen in the reduction of inflation and currency stability, have an adverse effects too. They are shown in reducing economic growth and employment, which could have negative impact on the economic system of euroized countries, in the long term.

d) Loss of the instruments of monetary policy and exchange rate policy

Under fixed exchange rates, the elimination of shocks requires changes in wages and prices, since in the absence of flexible wages and prices, the economy may fall into recession and a decrease in the economic growth. The country may face with inadequate nature of monetary policy in the case of divergent economic cycles and be unable to respond to the specific shocks or to supplement the fall of competitiveness (Boshkov, 2015). The euroized countries, despite the loss of running monetary policy, have no impact on the monetary policy of the ECB.

Euroization includes the risk of non-equilibrium exchange rate, which is even greater because there is no strategy of return. Any deviation of the real exchange rate from the equilibrium has negative effects on the interest rate, GDP, employment. In the absence of an independent monetary policy and instruments of monetary policy and exchange rate, there is increasing in the rigidity of wages and prices, thus increasing the costs in euroized economy.

e) Economic crisis

Structural characteristics of the country under unilateral euroization, play a key role in defining the balance of benefits and costs of euroization (Herrero and Glöckler, 2000):

1. the effects of reducing the risk of devaluation of the exchange rate will be greater in the countries with a tradition of high inflation and frequent currency crises;
2. great benefit from euroization will have small and open economies than large and closed countries, because small and open countries would increase the level of trade interdependence with the European Union;
3. advantage of eliminating the choice of exchange rate regime from the political debates will be greater in countries with strong lobbying and political incorrectness;

4. the absence of the option for moving out of unilateral euroization, will be less costly in the countries whose prices are more denominated in Euros and that are commercial and financial connected with the European Union;

5. cost of losing seigniorage will be low in the countries with a greater degree of currency substitution, since the demand for national money is small in those countries;

6. inability of the central bank to act as lender of last resort, causes less cost in the countries with strong and well-regulated banking supervision. Costs will be even smaller if there are other instruments for the regulation of banking crises, such as the broadcasting option bonds of public debt will represent a cash injection for the bank's liquidity.

There are a number of possible activities and guidelines that a country should adopt an unilateral euroization for accommodating the existing restrictions. First, in a weak banking system, the individual bank is in a difficult situation for independently adjustment, so by adequate efforts should be established a certain banking group. Secondly, this trend of concentration of banks, inspired by the growing share of foreign banks in the capital of local banks. In the absence of central bank and credit for liquidity, the insolvency of domestic banks amid crisis and shocks can be saved by the concerns of foreign banks for their capital. In the moment of pressure on bank liquidity, the internationalized banks can quickly and easily obtain foreign currency and secure their liquidity position.

Furthermore, due to lack of central bank supervision, it is necessary to establish an agency that will provide strict regulation and enforcement of banking supervision, so that interest rates will lead to a reasonable framework and improve the stability of the financial sector. Due to the danger of losing deposits in one bank can lead to disruption of the entire banking system. It is necessary to pass a law for the protection of deposits. Also, it is necessary to establish an institution that will act as lender of last resort, and whose foreign assets will amount to 100% of the reserve money. Of course, in the absence of policy exit it is necessary to define a clear exit strategy from the crisis, if this proves inevitable. The strategy should have several stages, starting from switching to another currency, or to create new instruments of economic policy, increasing the flexibility of the government, leaving the monetary rules and join some form of regional monetary integration.

Summing up all the advantages and disadvantages should be noted that unilateral euroization is one of the alternative forms of monetary authorities, which is recommended in conditions of hyperinflation, monetary instability and lack of credibility of the central bank as the creator of the monetary policy. The idea of introducing the euro in countries of Central and Eastern Europe initially perceived as a short path in the euro zone, while the European Union has not stressed that the introduction of the euro is not a sufficient condition for monetary integration and proposed three stages of monetary integration.

3. Estimating the Euroization

3.1. Methodology

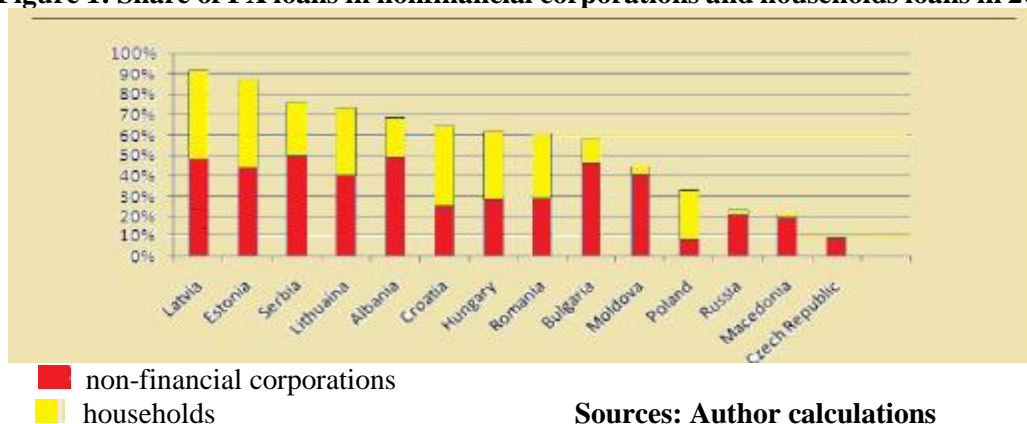
The analysis of the study is based on descriptive statistics and probit and ordered probit regressions as SPSS software. The estimation could be divided in three steps. First is the estimation of FX loans and its share in total private sector loans. Second, we estimate

FX loans and its currency denomination. Third, we estimate and show the relationship between FX-deposits and FX-loans.

3.2. Analysis, results and discussion

The degree of loan euroization determines the financial system's exposure to systemic credit risk in the case of large devaluations. As we mentioned above, the results show the share of FX loans in total private sector. For this purpose were taken non-financial corporations and households. From the figure could be seen that in Macedonia, Moldova, Poland, Croatia, Hungary, Romania, Bulgaria FX loans are denominated in foreign currency, while there are other country as Slovakia, Russia and Czech Republic where FX loans play minor role.

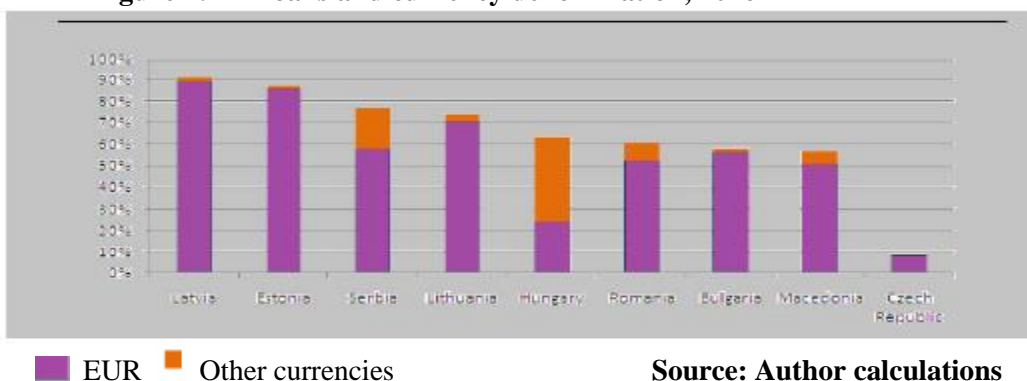
Figure 1: Share of FX loans in nonfinancial corporations and households loans in 2016



Sources: Author calculations

Next estimation is presented in Figure 2. Actually, we estimate currency denomination of FX loans. The figure 2 shows that, more than 90% of all FX-loans in the selected countries are denominated in Euro. The other currencies play minor role in the region.

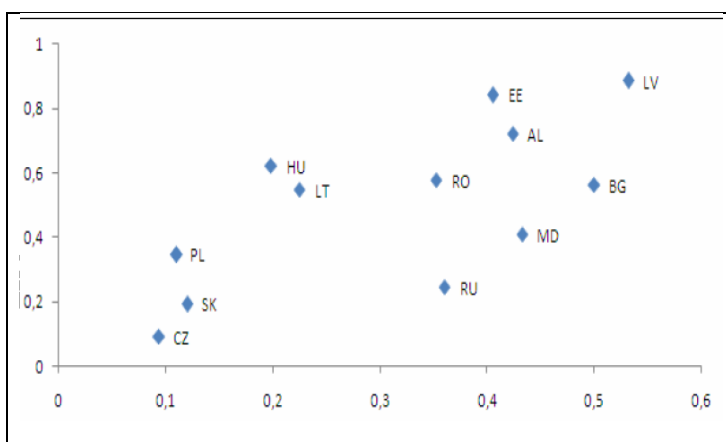
Figure 2: FX-loans and currency denomination, 2016



Source: Author calculations

Banks access to foreign funds determinates their ability to lend domestically in FX. Typically, most of them lend in foreign currency. This will increase the incentives for borrowing in foreign currency. Therefore, we ask an interesting question - are foreign banks more engaged in FX lending compared to domestic banks? The results show strong relationship between FX-deposits and FX-loans (Figure 3).

Figure 10: FX-deposits vs. FX-loans, 2016



FX-Deposits

Source: Author calculations

4. Conclusion

The focus in this paper was the causes of euroization in Macedonia. Beyond the incentives for de-euroization, Macedonia will remain euroized for a long time. The process of euroisation is a problem with a long history and usually persistent phenomena. The main driving forces in Macedonia are the experiences with the savings in the previous system, economic uncertainty in the transition period, external and internal shocks, private transfers inflows in foreign currency. Taking in account that Macedonia has fixed exchange rate peg to the euro, the confidence in the domestic currency is extremely important. The other facts are that foreign currency holdings are sensitive on economic and non-economic factors, increasing vulnerability of the economy. Also, there is need of regular monitoring of leading indicators in this field and proactive role of the central banks in managing the risks.

The evidences suggest that is difficult to reverse euroization. This is hard also when macro stability has been well established. There is some regional pattern of euroization and researchers think that it is related with the region economic integration into EU and aspiration for joining to the euro area.

The best strategy is to provide incentives and supportive macro-financial context for gradual reduction of euroisation, through prudential policies and by maintaining macroeconomic stability and developing domestic debt markets. Macedonia has been implementing prudent macroeconomic policies and has achieved macroeconomic stability in the last decade, including during the global financial crisis. Maintaining such a policy is a pre-requisite of de-euroisation. Given that the peg exchange rate has limited the scope of monetary policy to respond to inflation, fiscal policy could play a larger role, including by improving public debt management and relying more on longer term denar loans. This would be an important step in fostering the development of domestic debt market. A deep and liquid domestic capital market could provide more investment opportunities in denar as a substitute for FX-denominated assets, thus helping the de-euroisation.

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