

FY 1999 FOURTH QUARTER
PROGRAM REPORT

July 1, 1999 to September 30, 1999

**Strengthen Private Enterprises in War-Affected
Areas of Croatia**

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PROGRAM OVERVIEW

Highlights

- **0 52% Decrease in employment with assisted firms**
- **4 96% Increase in sales with assisted firms**
- **5 New agricultural associations organized and registered**
- **192 New members in assisted associations**
- **45 New business linkages**
- **1907 Consultations with private businesspersons and farmers**
- **7 seminars with 233 Participants**
- **14 Visiting technical advisors**

FY99 FOURTH QUARTER RESULTS

The growth and expansion of FLAG clients in the war affected areas of Croatia continues to facilitate the reintegration of war affected populations. In a challenging economic environment, FLAG SME clients in the war-affected areas continued to outperform the overall economy **with sales increasing by an average of 4 96 percent** compared to the corresponding period the previous year. The Croatian economy continued to struggle and is currently in its fourth consecutive quarter of recession. GDP decreased by 0 6 percent compared to the corresponding period the previous year and industrial production in particular does not show signs of recovery. At the end of August 1999, industrial production had declined by 2 8 percent compared to the corresponding period in 1998 ¹

Despite these negative economic trends, FLAG SME clients in the war-affected areas of are almost maintaining current employment levels and only averaged a **0 52 decline in employment** compared to the corresponding period the previous year. At the end of August 1999, registered unemployment in Croatia was 19 1, which is 14 2 percent higher than at the end of August 1998. In addition to rising unemployment, there are still an estimated 150,000 employed workers who are not paid regularly.

Many FLAG clients are involved in agricultural production and processing. Agricultural production and processing was 8 4 percent lower at the end of August 1999 compared to August 1998 ². Another cause of the downturn in the Croatian economy is the poor performance of the traditional export industries and weak domestic demand. Personal consumption has declined by 11 percent in 1999 compared to 1999 ³. FLAG SME clients continue to be affected by weak domestic demand and rising inter-company arrears. FLAG continues to promote exports and has facilitated **45 linkages** for our SME clients to boost export sales to non-traditional markets. FLAG clients continue to target Croatia's largest export market, the EU. Promoting exports will reduce the effect of weak domestic demand and avoid increasing receivables caused by large inter-company arrears. FLAG will also initiate a new value added electronic commerce service for SME clients during the next quarter to continue our emphasis to promote regional trade and exports.

¹ Croatian National Bank, Bulletin No. 42, October 1999

² Ibid

³ Ibid

FLAG has organized and **registered 5 new agricultural associations and cooperatives** during this quarter, bringing **the total number of active associations and cooperative clients to 22** (21 agricultural associations and cooperatives and 1 SME association) FLAG will now refocus technical assistance on strengthening existing association clients to expand membership and ensure sustainability Our emphasis on registering and organizing new associations and cooperatives has been successful and our emphasis will now shift toward strengthening and expanding existing clients To date, **membership has increased to 11,742 during this quarter**, an increase of **192 new members** over the previous quarter In the rural areas of the war-affected areas, agriculture represents the most significant employment opportunity for returnees Table 1 illustrates progress towards annual goals

Table 1 – Targets and Indicators

INDICATOR #1

ENTERPRISE GROWTH AND EXPANSION

TARGETS		4 th quarter FY 99
1 1	15% sales growth in assisted firms	4 96%
1 2	10% employment growth in assisted firms	-0 52%
1.3	30 assisted firms	53

53 * sales growth and employment growth for Jan 1st 1999 to Sept 30th 1999 compared to the same period of the previous year

INDICATOR #2

REINTEGRATION OF THE REGIONAL ECONOMIES

TARGETS		3 rd quarter FY 99	4 th quarter FY 99
2 1	150 transactions linking enterprises in formerly occupied regions to Croatia and abroad	229	274

* Linkages counted from October 1st 1998 to September 30th 1999

INDICATOR #3

COOPERATIVE AND ASSOCIATIONS DEVELOPED

TARGETS		3 rd quarter FY 99	4 th quarter FY 99
3 1	8 new cooperatives or associations developed	23 (cumulative)	33
3 2	10% increase in revenue of assisted cooperatives and associations	n/a	19 12%

☆ increase in revenue of assisted cooperatives between Jan 1st 1999 to Sept 30th 1999 compared to the same period of the previous year

INDICATOR #4

POLICY AGENDA ISSUES ADDRESS LEGAL AND REGULATORY CONSTRAINTS TO SME DEVELOPMENT IDENTIFIED AND SOLUTIONS PROPOSED BY ASSISTED COOPERATIVES AND ASSOCIATIONS

TARGETS		3 rd quarter FY 99	4 th quarter FY 99
4 1	3000 benefiting cooperative or association members	11,550	11,742

FIRM LEVEL ASSISTANCE

FLAG Croatia completed 14 volunteer and consultant assignments and 7 seminars during this quarter with 233 participants. 4 new clients were added to our portfolio, which now includes 37 active business clients that receive technical assistance from resident expatriate advisors, local business and agricultural advisors, local consultants, and US volunteer advisors. More than 1,907 consulting meetings were conducted with clients by US volunteers, resident expatriate staff, and local business and agricultural advisors. SME clients are slowly expanding despite the poor environment and the limited support provided by local financial institutions and ministries.

ASSOCIATION ASSISTANCE

Agricultural production and processing provides an important source of income for many returnees in the rural parts of the war-affected areas. FLAG currently has 22 active agricultural association and cooperative clients, after adding 5 new clients during this quarter. Membership has increased to 11,742. In the past, FLAG has implemented a grass roots campaign to organize and register associations and cooperatives in the war affected areas, and to focus on marketing assistance, production scheduling, and budgeting. This effort has been a success. Beginning in the next quarter, FLAG will focus fewer resources on registering associations and cooperatives, and will concentrate more resources on marketing assistance, production scheduling, budgeting, and accounting.

Pending approval of Modification 06 (Modification 05 was a no cost extension to bring the Montenegro component in-line with the existing Croatia Cooperative Agreement end-date) to the existing Cooperative Agreement, FLAG is preparing to implement a new grant fund to capitalize agricultural cooperatives and associations. The goal of the grant funds will be to provide support for refugees and displaced persons using innovative funding strategies for economic development projects in the war-affected areas of Croatia. Projects will be built around market opportunities for primary production and processing of agricultural commodities. Grant funds will be used to promote economic development, and when appropriate, in collaboration with other USAID implementers and International Organizations. The grant funds will provide timely, beneficial economic support for returnees and persons affected by recent conflicts in the Balkans and the communities where they have returned in recent years and where more are likely to return. The objective is to leverage technical assistance with grant funds to promote local economic development projects from our existing client base.

World Learning organized the third Cooperative Leaders TRANSIT program in the US from August 14th until September 5th. The group of 14 Croatian association and cooperative leaders from the war affected areas participated in the USAID sponsored 3-week training program in Missouri. The implementing organization in the US was the Jefferson City Missouri based International Consulting and Business Training (ICABT), associated with the University of Missouri's International Agriculture Programs and University Extension. The training included visits to the electric cooperative and research farms of the University of Missouri. On September 22, 1999, at the Hotel Palace Zagreb, World Learning organized a one-day post-program briefing and follow-on workshop. FLAG continues to work with each of the participants in the field, some of whom are managers of FLAG client cooperatives and associations.

PRIVATIZATION ACTIVITIES

FLAG continued its pilot privatization project with five limited liabilities companies in the war affected areas. The goal is to initially secure jobs, restructure the companies and create healthy private companies that will begin creating new jobs in the war affected areas. The project includes facilitating the privatization of under-performing assets of two Holding Companies, *BOROVO JSC* and *IPK JSC*. *BOROVO* registered three new daughter companies in June 1999, but the Holding company retains 100 percent ownership of its assets. *IPK* registered two new daughter companies in May 1999 and also still retains ownership of all assets. The five daughter companies are managed by entrepreneurs who have requested FLAG assistance privatizing and restructuring their companies. A privatization team consisting of one expatriate and one local advisor will manage the pilot projects out of the FLAG Osijek office.

To date, FLAG has signed a Memorandum of Understanding (MOU) with two of the daughter companies of *IPK, Daljska Polja* and *Erdutski Vinogradi*, and has agreed on a draft MoU with the three daughter companies of *BOROVO*, Borovo GTR, Borovo Leather Footwear, and Borovo Rubber Footwear

FLAG will draft a Scope of Work in the next quarter to recruit a team of US Executives that will conduct a feasibility study for each Borovo daughter company. The executive team will also recommend restructuring the companies and draft a preliminary lease agreement the daughter companies will submit to Borovo Holding

POLICY REFORM

US consultant, Jane Shey, completed an assignment with the Union of Associations of Slavonija and Baranja in July 1999 and drafted an agricultural policy reform paper for the association. The final draft of her reform paper is attached. The goal of her assignment was to assist with the preparation of an agenda for the association, which will be used by the association to recruit new members and to begin dialogue with the Government to advocate policy reform. During the next quarter, FLAG will concentrate technical assistance on institution building within the association, which has a loosely organized management structure, limited information flowing to its members and an overall challenge managing its rapid growth and focus on lobbying activities

Jim Rathbun completed a two-week assignment in September with SMEA, a national SME association headquartered in Zagreb. The goal of the assignment was to identify major issues negatively affecting the SME community and to draft a summary platform that recommended possible solutions to these issues. Rathbun's final report is attached. FLAG intends to work closely with SMEA to develop the initial draft into a comprehensive document that SMEA can use in future dialogue with government officials and to recruit new members in order to eventually lobby for changes. During the next quarter, FLAG technical assistance will also concentrate on institution building and a membership campaign

Both Jane Shey's and Jim Rathbun's policy papers will be an integral component of a World Learning sponsored in-country training program scheduled for 12-16 October, 1999. The October program will provide training to national and regional association leaders to improve communication between the diverse associations representing agricultural producers and processors. The goal of the program is to begin formalizing lobbying campaigns and institution building among each association

OUTREACH PROGRAMS

FLAG continued to provide outreach programs to the local SME and agricultural community

- In conjunction with the Union of Associations of Farmers in Slavonija and Baranja, FLAG developed and published the second and third edition of an agriculture newsletter. *The Agricultural Messenger* was printed in July and in September. Both issues are attached and were distributed through all existing FLAG associations and the local agriculture advisory offices
- FLAG Daruvar appeared in a "Hrvatska Danas" feature on national TV in a segment filmed at the HREŠIĆ facility in Daruvar. The segment lasted about two minutes and included general information about FLAG Croatia

- The Jutarnji List newspaper cited FLAG's support in the formation of the Đulovac Sheep Breeders Association
- FLAG Petrinja appeared in TV news featuring interview with FLAG volunteer James Skip Meneely while on the assignment at KORDUN JSC, a FLAG Petrinja client in Karlovac. The segment lasted about two minutes and included general information about FLAG Croatia
- On September 9th FLAG Petrinja sponsored the "Big Ag Meeting" on the premises of Gavrilovic's canteen. The seminar was attended by approximately 120 guests, mostly farmers associations members from all over Croatia, including their leaders and deputies, Union Of Coops, numerous agricultural companies, marketers and a great number of NGOs. Chief Of The Party Mr Mark Grubb delivered a speech on FLAG efforts towards the platform for reform in agriculture. The opening statement was delivered by Mr Gjuro Gavrilovic in which FLAG was outlined as the great cooperate and benefactor assisting Gavrilovic Ltd in reaching the potential supply market, making technological links and making available the volunteer expert (VE) on HACCP standardization, Mr Fred W Billerbeck

UPCOMING ACTIVITIES

During the next quarter, FLAG will initiate a new local economic development grant that will capitalize agricultural cooperatives and associations in the war affected areas. The grant projects will be leveraged with technical assistance from FLAG advisors, local consultants, and volunteer advisors. SME clients will be introduced to the GTN electronic commerce system, which will provide additional services FLAG is already providing to increase exports and to facilitate regional trade. FLAG national and regional association clients and potential future clients will participate in a World Learning organized in-country training seminar.

- ✓ The following seminars are planned for the next quarter
 - seminar on hog breeding for the association in Badljevin
 - seminars for sheep and goat breeders on parasite control
 - seminar on mastitis and somatic cells for dairy farmers
 - seminar on Cooperative Advantages in Grubišno Polje
 - Marketing seminar for FLAG SME clients in Sisacko Moslavacka and Karlovacka region conducted by professor Hitrec, the honorary lecturer at the University Of Economics and one of the founders of SMEA. The seminar's main theme will be standardization of domestic products towards the foreign markets and systemization of the domestic & foreign marketing ways
- ✓ FLAG Daruvar intends to organize the following events for its clients
 - "Days of Honey" for the "BAGREM" Association. It will be a 7 day event with exhibitions throughout the week at the beginning of December
 - "Day of BIOGAL" will be organized to promote BIOGAL's new home delivery service next quarter

FLAG Vukovar – Osijek / Former sector East

Quarterly Report

1 July – 30 September 1999

I Significant Events

- Three FLAG volunteers provided technical assistance to five business clients and three agricultural clients this quarter
- The cattle feed and hog producer, **PROTEIN**, reported that it has more than doubled its number of employees since becoming a FLAG client
- FLAG has worked fervently this quarter with members of the agricultural association, **BIOPROTEIN**, to create By-Laws, a Charter and all necessary documentation for registering the cooperative, **ACAŠ**. The new cooperative will initially be comprised of 23 members and will specialize in hog production
- Volunteer Lew Dow fulfilled a six-week management assignment with three agricultural cooperatives. He provided technical assistance in organizational and budgetary issues, and operations management
- Volunteer John Gauthier completed a six-week marketing assignment with four of FLAG's business clients
- Volunteer Robert Zeldenrust concluded a two-week assignment with the cattle feed and hog producer **PROTEIN**. He provided assistance in developing pricing, sales and marketing strategies for the company

II Business Highlights

Clients

STROJOREMONT Employs five people in Borovo Naselje and offers the following services, renovation and servicing of used rubber processing equipment, and the production of rubber spare parts for agricultural equipment. FLAG volunteer, John Gauthier, provided marketing assistance as well as established a contact with *Norchris Associates*, a US brokerage firm. *Norchris Associates* has recently prepared a draft of a contract to represent Strojoremont and market its products in North America. FLAG has contacted *Skoda Auto Corporation* regarding the purchase of rubber spare parts from *Strojoremont*. *Skoda's* Purchasing Department has included *Strojoremont* in its database of suppliers and will consider the company's services in the future. *Strojoremont* has recently implemented a FLAG marketing proposal by placing advertisement billboards along roads in the region.

MI-NI Employs 16 people in Borovo Naselje and provides shoe-sewing services to footwear companies. FLAG has assisted *MI-NI* in creating company business cards and is currently developing a company brochure and web-site. FLAG traveled to Italy this past August and offered *MI-NI's* services to four Italian footwear companies. Afterwards, FLAG worked jointly with *MI-NI* in submitting contract proposals to sew shoes for these Italian companies. FLAG's

and *MI-NI s* combined efforts have resulted in the Italian footwear company, *Stilman*, contacting *MI-IN* regarding possible future cooperation FLAG has also made arrangements for *Prusina Auditing Company* to audit and provide financial consultation services to *MI-NI*

PROTEIN Cooperative has 18 employees in Bobota and produces livestock feed and hogs *Protein* has maintained its sales levels from the previous year and has recently increased the quantity of pigs raised over the past quarter by 10% FLAG has aided *Protein* in contacting the large Croatian meat processor, *Gavrilovic*, in an attempt establish a more reliable customer for *Protein s* hogs FLAG has also arranged for *Prusina Auditing Company* to audit and advise *Protein* regarding Croatian accounting and tax regulations

PILE Hatchery and producer of one-day-old chicks with 6 employees in Brsadin In the past few months the company consistently increased the quantity of broilers produced Currently, *Pile* produces 15,000 broilers (over a 2-month period) on three farms in the surrounding villages *Pile* has begun producing its own feed in accordance with the recipes provided by FLAG's Least Cost Feed Formula These measures have resulted in a significant decrease in cash outflows (i.e. 35% reduction in feed costs), and at the same time have improved *Pile's* feeding ratio and the productivity of its layers (5% increase) In the upcoming quarter FLAG plans to continue to assist *Pile* in developing marketing material and to provide *Pile* with a veterinarian volunteer

MATURUS Manufactures wooden doors, windows, furniture and staircases in Borovo Selo with 16 employees FLAG has assisted in marketing *Maturus s* products to Norwegian, Austrian and Italian companies The company is presently taking measures to implement the marketing advice provided by volunteer John Gauthier In January 2000 *Maturus* will advertise its services in the first Croatian catalogue specializing in wooden doors and windows FLAG will continue to work closely with *Maturus* in creating a more aggressive marketing plan as well as provide assistance in developing a company price list, brochure and web page

PVC KELAVA Producer of PVC doors and windows with six employees In September the company commenced operations again in Mirkovci after moving its assets back from Bjelovar FLAG is currently assisting *PVC Keleva* in the implementation of a marketing strategy suggested by volunteer John Gauthier which includes designing a company trademark and catalogue, researching other products that can be made from PVC, accepting checks and credit cards as means of payment, opening retail shops, and selecting several distributors to market its products throughout Croatia FLAG will also support *Maturus* in exploring the possibilities of designing indoor swimming pools and greenhouses

II Agricultural Highlights

Clients

RIT AGRICULTURAL COOPERATIVE (Bilje) Agricultural cooperative with 77 members, who are all residents of the Bilje municipality in Baranja FLAG graduated the *Bilje Association* as a client and signed an MOU with the *RIT Cooperative* last quarter The cooperative was approved by a Norwegian government funded organization to be the recipient of a 1.7 million DEM credit program Unfortunately, the Norwegian credit program in Osijek-Baranja County has been postponed indefinitely However, a Norwegian representative has recently promised the *RIT Cooperative* some credit for the upcoming year and has invited the

Cooperative's manager to Norway to discuss the credit program in detail A/V volunteer Lewis Dow completed a training assignment for *RIT Cooperative's* management in managing the cooperative's daily operations more efficiently and effectively A/V volunteer Douglas A York will be heading a feasibility study of the possibilities of cold storage and vegetable production for the *RIT Cooperative* this upcoming quarter Also, FLAG will continue to work with the cooperative in preparing a marketing strategy for next year

BARANJA DAIRY FARMERS ASSOCIATION (BDA) Association will market dairy products for farmers in Baranja More than 300 farmers have completed applications to join the association During this quarter, the *BDA* collected 137 membership fees Also, *BDA's* Supervisory Board recently met with the management of a local milk processor, *Agrokombinat Belje*, regarding delinquent payments by *Belje* to *BDA's* farmers for milk (the farmers have not been paid in 6 months) *BDA* and FLAG are currently working on a two-pronged strategy to collect receivables from *Belje* and to begin building the infrastructure necessary to gather and deliver milk to another processor

BIOPROTEIN Agricultural association with 105 members in Vera 23 members of *Bioprotein* are in the process of registering the cooperative *ACASŠ*, which will specialize in hog production During this quarter a representative from the Croatian meat processor, *Gavrilovic*, visited a few of *ACASŠ's* hog farms and was very impressed with the quality of the hogs Volunteer Lew Dow assisted in preparing a budget for the cooperative's first year of business FLAG is currently collecting financial data to determine *ACASŠ's* expected cash flows for the upcoming year FLAG is also making projections of *ACASŠ's* costs for raising hogs through all stages of development (i e from piglets to market weight) FLAG plans over the course of the next quarter to assist *ACASŠ* in searching for financial support for the cooperative's initial start-up costs FLAG will prepare a database of *ACASŠ's* members and will continue to develop relations between *Gavrilovic*, and *ACASŠ* with the final goal of a contract being signed between the two parties

NAŠE SELO Agricultural cooperative in Jagodnjak has 75 members with 10 full-time employees FLAG has contacted eight Croatian companies (i e mills, bakeries, etc) in an attempt to find potential buyers for *NAŠE SELO's* wheat Volunteer Lew Dow advised *NAŠE SELO* on making necessary changes to the cooperative's bylaws for when it becomes fully privatized *NAŠE SELO* has not received the expected loan from a Norwegian organization and therefore, has been forced to postpone its plans to construct a workshop for the maintenance and repair of farming equipment As soon as *NAŠE SELO* is registered by the Croatian authorities as a private cooperative, FLAG will be able to provide more concrete technical assistance to the cooperative

ILOK Agricultural Association of 39 members in Ilok with five members specializing in grape production These grape producers are currently negotiating with Austrian investors to develop a vineyard for wine production in Ilok FLAG has provided these members with information regarding investment regulations for foreign investors in Croatia If the association members receive financial support from Austria, FLAG will engage in market research and provide technical assistance for the wine production project in Ilok

III Coming Events

- Volunteer Douglas York will be arriving in October for a one-week assignment to provide technical assistance in vegetable production, cold storage and marketing for FLAG s agricultural association and cooperative clients

FLAG Daruvar / Former Sector West

Quarterly Report 1 July – 30 September 1999

I Significant Events

- Mr Stefan M Peterson resigned from his position as a Regional Director for FLAG Daruvar. His position was assumed by Mr Greg Olson on October 4. Mr Olson graduated from the Darla Moore School of Business at the University of South Carolina (Masters of International Business Studies, MIBS). Prior to business school, Mr Olson worked as an investment analyst assistant in Costa Rica and with the Small Business Development Center in Columbia, South Carolina. Mr Olson also has management experience obtained while working with several private business firms in France.
- The FLAG Daruvar outreach program included the following events
 - The Daruvar Team appeared in a "Hrvatska Danas" feature on national TV in a segment filmed at the HREŠIĆ facility in Daruvar. The segment lasted about two minutes and included general information about FLAG Croatia.
 - The Jutarnji List newspaper cited FLAG's support in the formation of the Đulovac Sheep Breeders Association.
 - Volunteer Expert (VE) Toney Reynolds gave seminars on hog, sheep and cattle management to IRC beneficiaries in the Okučani Municipality. 14 people - primarily returnees and IRC beneficiaries - attended the seminar.
 - Volunteer Expert (VE) William Lord gave a seminar to the Beekeepers Associations in Daruvar and Bjelovar. Both seminars had a very good attendance with an average of 50 people at each event.
 - Daruvar Advocate Nada Kožul went for the opening ceremony of "Susret", a drug rehabilitation center, where she met Mr Juro Radic, Minister of Reconstruction and Development for Croatia.
 - Daruvar Advocates Oljeg Papac and Mirsada Vatrač went with Volunteer Executive (VE) Jim Rethbun to a roundtable discussion about the development of Badlješina, where they met Mr Anto Bagaric, Head of the Požeško-Slavonska County.

II Business Highlights

Overview

Not much has changed in the business environment during this quarter. Companies still faced the same problems of limited access to loans, with interest rates hovering between 15-26% for short term loans. The fact that the VAT must be paid to the government 30 days after invoices are issued and not when payment is actually collected presents another big challenge for the companies' cash flows.

While the government itself can afford to not pay its debts towards companies, it is requiring that companies regulate their obligations towards the government promptly. Some entrepreneurs are trying to convince the government to break down the debts and disregard the VAT payments or the companies' tax on profits. In return, they would write off the government's debt toward them. Unfortunately, the Ministries of Health, Agriculture, and Reconstruction and Development are not in favour of this solution, leaving the companies with only one solution – to sue the government.

None of our clients have received a loan approval. At the same time, they have simply stopped asking for loans intended to expand their production capabilities.

Even our clients who are exporting faced certain difficulties during this quarter. POD and MPD had to reschedule their plans to reenter markets in the former Yugoslavia due to the NATO bombing campaign. Even though they had shipments of goods waiting to be sent, they could not send them and lost a lot of money, which was tied up in inventory. POD also had difficulties with the Slovenian government's introduction of a VAT in July of this year. Again, this resulted in a delay or cancellation of orders and shipments. The BiH government decided to cancel the free trade agreement between BiH and Croatia which had previously allowed companies to pay only 1% in customs duties on its exports to Bosnia. This increased the price of products made in Croatia and made them less competitive in the BiH market.

The government continues to use bills of exchange to pay for part of its debt towards suppliers or contractors working with certain Ministries. Even though many companies had serious doubts that they would ever be able to get the money from these bills, the banks exchanged them with different discount rates and conditions (usually 20-30% interest per year plus mortgage). Those who waited did get their money directly from the government in due time.

Even though the overall economic situation seems grim at the moment, there are signs that things will get better. One of these signs is the Business Incubator Project started by the town of Pakrac. With the help of the Požeško-Slavonska County and one Dutch advisor, Pakrac applied with the World Bank and received money for upgrading the infrastructure in the future industrial zone.

The town of Pakrac has two projects underway to stimulate business in the area. They plan to build a Business Incubator, i.e. reconstruct one building in the town itself where they would situate small businesses and crafts. In this Incubator, the businesses and crafts would be able to use services such as phone and fax, and receive legal and financial advice. All of these services would be free of charge in the beginning. Only later (about 5 years) would the town charge a small fee in order to continue financing the project.

The second project is the previously-mentioned Industrial Zone. The town of Pakrac has a big industrial park containing the Papuk Wood Industry. This was heavily damaged during the war but still has all the necessary infrastructure elements in place, including a railway. The town plans to use a World Bank loan to upgrade the facilities and to offer them to medium-sized companies for their own use as office space, warehouses, etc.

Clients

This quarter FLAG Daruvar continued to support its 11 business clients and adopted 2 new ones

Babur Start-up business collecting wild mushrooms and snails, 1 employee They still do not have their own sales force due to a lack of working capital and are collecting mushrooms and snails this year as a sub-contractor for bigger companies They currently have small profit margins BAC assistance offered to put them in touch with a SEAF client, "GLJIVA" Both companies were interested in the partnership However, we will have to wait for the season to end for the final results This company's biggest problem remains their loans, which they have not been able to repay

Biogal Milk processor in Daruvar, 8 employees Following the advice of one VE, the company has continued developing new products and services One of these products, a clotted cream, was introduced this quarter and has been selling well After a long entanglement with bureaucratic red-tape, the company has managed to obtain all the permits needed to begin its home delivery service, which began on October 1, 1999 FLAG Daruvar helped Ms Pokorny, the owner, locate fruit juice concentrate and fruit paste producers in Europe FLAG Advocate Nada Kožul will join Ms Pokorny at the CEI (Central European Initiative) conference which will be held in Brijuni later in October BAC assistance in the following quarter will include helping to create brochures advertising the company's services, marketing its home delivery service, and helping to organize a promotional activity (called BIOGAL DAY) in Daruvar, including air-time on the radio, a stand at the outdoor market, etc

EccoTherm Heating and air conditioning design and installation in Daruvar, 14 employees After the general manager's return from EMED, FLAG Daruvar continued communicating with the US HVAC Association However, due to the overall economic situation in the region, the company has been having problems with its day to day operations, and its plans to form a Croatian HVAC Association had to be postponed In order to help the company cut down on its operating expenses, we suggested dividing the business (keeping the maintenance sector in Daruvar and the administration in the Pakrac Business Incubator This has not yet been accomplished but is being planned) BAC has had discussions with EccoTherm and members of the Incubator of Incubator and is going to keep working on forming a Croatian HVAC Association

Hrešić Meat processor in Grubišno Polje, 13 employees VE Hillyard completed his one month production/marketing assignment with the company to mutual satisfaction He provided numerous recipes for different types of sausages and other meat products using soy protein and surplus fat The cooperation resulted in the trial production and sale of eight new sausage products VE Hillyard suggested conducting a brief follow-up within 12 months VE Reynolds also visited the company and promised to supply Mr Hrešić with recipes for hog feed which Mr Hrešić could use on his farm

Korina Agribusiness in Novska, 45 employees They completed their plans for harvesting grain and began preparing for the sowing season They increased their cooperation with farmers by offering them slightly lower prices for drying and storing grain per VE Kabot's advice Through FLAG's assistance, they are increasing the number of farmer cooperants in the hog finishing business

Metaflex Metal processor in Novska, 120 employees A Norwegian NGO met with the company's management and discussed the potential exchange of lumber for used sawmill equipment Even though the Norwegians were interested and showed a lot of trust and confidence in Metaflex's management, they could not make any deals because Metaflex was unable to show them specimens of finished products We will continue looking for other sources of financing for Metaflex

MPD Pump manufacturer in Daruvar, 118 employees Dissatisfied with the company's management, the employees organized another labor strike and banned Mr Shejbal (manager of the company) from entering the company's premises This resulted in a change of management VE Gauthier provided a list of pump distributors in the US (New England area) But, due to MPD's financial difficulties and unstable management, the company did not follow up on these leads We are going to estimate our future cooperation with this company in the next quarter

POD The sales manager traveled to the US to meet with the US spring manufacturers and other farm equipment dealers After we provided them with LIFAM contacts (a FRY-based company), POD began preparations for export to the FRY, but the shipment was delayed due to NATO bombings With BAC assistance, POD sent an offer for tractors and other farm equipment to a Sofia-based Swiss NGO working in Kosovo but has not yet receive a reply

SAB Metal processor in Daruvar, 12 employees As a result of a marketing volunteer visit, BAC will provide the SAB management with materials that the VE had collected while researching the US market for SAB products However, considering that we did provide SAB with all aspects of our technical and other assistance and received a very poor return of information from the management, we are seriously considering graduating the company in the next quarter

Samtex Textile crafts in Lipik, 1 employee Through BAC assistance, Mr Stojic has re-registered his business and can now sell his products directly in retail The BAC also assisted Mr Stojic in searching for raw material suppliers so that he could become more independent (he's currently contracted by MIKAS, which gives him the raw materials (excess cotton filament) with which he makes rugs Then, he sells the rugs back to MIKAS for a very low price—well below the market value) SAMTEX still did not move into the business incubator due to Pakrac's financial difficulties

Usluga Manufacturer of playground equipment in Pakrac, 8 employees Mr Turuk was not available during the summer season due to his work on the coast The client is planning to expand his workshop in the coming months

New Clients

Norma Coffee roaster/grinder manufacturer in Daruvar, 4 employees and several local subcontractors such as MPD BAC continued to support this company's search for potential US partners in conjunction with the EccoLinks project (EccoLinks was supposed to give money for a study regarding reducing Norma's waste products) However, the EccoLinks funding did not come through do to the fact that the potential partner which we found did not come through with its support BAC will continue helping Norma's search for US producers of afterburner devices The company's management has been considering the possibility of producing small soy bean toasters for family farms and asked for our assistance in researching this subject We

provided them with information regarding technical details on toasting soy beans and will continue providing support for this project in the future

ANTIĆ Custom furniture maker in Nova Gradiška, 6 employees The piggyback marketing VE Jansa researched the US market and informed the management that their product would be competitive in the US even when including the cost of shipment The BAC helped the company develop two possible marketing strategies for Croatia one uses a web site, and the other uses billboards located at the entrance to the Zagreb airport System Administrator Boris Pran has nearly completed the web site, and we are still studying the use of billboards

III Agriculture Highlights

Overview

The problems in the agricultural sector remain unchanged throughout this quarter Returnees of Serb nationality are still mostly elderly and live off of humanitarian aid, depend on donations made by IRC, UNDP, HelpAge or Red Cross, and, unless ASB has reconstructed their houses, live in a very poor conditions All the donations that they received are small and consist of small amounts of money, such as a 6 000 Kn grant made by IRC for livestock or mechanization purchases, or of livestock donations, such as HelpAge's contribution of 5 sheep, 10 chickens, and a sow per family UNDP has started a loan program for returnees to stimulate agricultural production However, the money received cannot be used to purchase mechanization or to reconstruct farm facilities – it can only be used for production itself (buying seed, livestock, fertilizer, etc) The amount of the loan and the repayment period vary, depending on the project, while the interest rate is set at 7%

Returnees of Croatian and/or other nationalities suffer from different but substantial problems The government has rebuilt some houses but has not provided any funds for reconstructing farm buildings Considering that many companies have stopped working due to significant amounts of war damage or are working below capacity, many people have had to turn to farming They have taken out loans to purchase equipment, rebuilt stables and barns, or invested in livestock, but are currently facing marketing difficulties because of the country's import policies and the overall illiquidity of the economy The government has promised subsidies for certain products such as wheat, barley, soy beans, milk and cattle, however, it is not paying them in time People who have taken out loans were counting on those subsidies and are now facing the possibility of losing their property because they cannot repay their loans

All of this fueled the farmers' anger, leading them to set up road blocks at the end of the last quarter and the beginning of this quarter This protest, in turn, caused the government to start paying the promised subsidies

Clients

Badljeva Association 18 members BAC linked members of the association with HelpAge, an EC-funded NGO that is providing returnee beneficiaries with livestock and other household items HelpAge was looking for hog suppliers (sows up to 60kg), and we referred them to this association This resulted in a 54 000 Kn sale for the farmers and attracted 6 more members to the association Veterinarian VE Toney Reynolds met with the members of the association and made some recommendation regarding feeding and general upkeep BAC linked them with the client Hrešić which again resulted in 20,000 Kn worth of sales, and we linked them with

companies importing and selling components for feed We invited the president of the association to a Petrinja agricultural event which resulted in linking him with our other clients such as NEŠIĆ Bijelo Brdo and Mr Petričević from Agroslavonija

Dulovac Association 70 members, including 15 minorities and 1 Kosovo Croat After meetings with members of the association, FLAG decided to work with some of them and slowly graduate this association as a client The members with whom FLAG decided to continue working were sheep breeders who took some of FLAG's suggestions seriously and formed their own Sheep Breeders Association

Dulovac Sheep Breeders Association 10 members, formed per our suggestion and guidance FLAG helped them with the registration paperwork and provided VE assistance regarding general upkeep of animals Two members of the association won prizes for their sheep at the State Agricultural Fair in Gudovac BAC provided help with making a brochure for the association and will sponsor a visit for the group's secretary to a seminar on sheep breeding in Poreč in October

Prekopakra Fruit Growers Cooperative 7 members As mentioned in the highlights, after registering their cooperative, the members faced an impassible roadblock in finding financing for a cold storage facility We continued our work in this direction and recommended the cooperative to people running the Pakrac Industrial Zone Project with the hopes that they would be able to finance the cold storage or at least provide the cooperative with some business premises

Gornji Bogicevci Goat Association 10 members This association was formed with FLAG assistance However, not all of the paperwork has been completed Their registration permit has not yet been issued, so the association has not officially started to work However, FLAG nominated the secretary of the association, Mr Petričević, for TRANSIT, which he has successfully completed BAC intends to work more with the association after they receive the registration permit and complete all other necessary administrative work

Beekeepers Association "BAGREM" 50 members VE William Lord provided technical and marketing assistance to this association and gave a very successful seminar to its members BAC linked members of the association with KRAŠ, the largest Croatian candy and chocolate producer who is interested in buying larger quantities of good quality honey

Events

- Visited Dr Matotan from PODRAVKA and arranged for him to prepare a greenhouse production feasibility study for Dragalić The study was completed and shared with other offices We also visited a successful producer of greenhouse vegetables in the Varaždin area and ensured that the greenhouse production is a feasible operation Funding for the greenhouse project and cash flow analysis remains to be secured
- Started cooperation with new Grubišno Polje mayor, Mr Zlatko Mađeruh The previous mayor did not want to work with NGO's or IO's, but, Mr Mađeruh has proven to be very cooperative He is interested in technical assistance to create feasibility studies for the use of abandoned farmland
- We met with the dairy company "SLAVIA" from Staro Petrovo Selo to discuss the potential purchase of milk from around Okučani This dairy currently buys goat milk from that area

They are interested in buying cow milk as well and are willing to set up cooling tanks if there is a sufficient supply

- Three candidates for TRANSIT successfully returned with plans for the future development of cooperatives FLAG Daruvar will continue to work with the 3 candidates on their plans

IV Upcoming Events

- FLAG Daruvar will continue to identify SME's having potential to impact the return process with technical assistance In the weeks ahead, the BAC will evaluate signing MoU's and recruiting VE's for the following companies
 - Pčelarstvo Daruvar honey packaging operation with 4 full-time and 4 part-time employees The BAC has identified this company as having a huge potential for developing beekeeping in the area as per VE William Lord's advice The company is also a potential SEAF investee
- FLAG Daruvar is currently working with several farmer groups in the process of creating associations Assistance includes organizing the first meetings and preparing registration paperwork In the coming months, we anticipate forming the following associations
 - Novska free-range hog breeders association with members throughout Croatia
 - Pakrac sheep farmers association
 - Grubišno Polje farmers association/cooperative
- FLAG Daruvar intends to organize the following events for its clients
 - "Days of Honey" for the "BAGREM" Association It will be a 7 day event with exhibitions throughout the week at the beginning of December
 - "Day of BIOGAL" will be organized to promote BIOGAL's new home delivery service next quarter
 - Gathering of hog farmers from the Western Slavonia area in Pakrac where we will promote our hog farmer clients and link them with other hog farmers, feed producers, and equipment retailers this november
- The following seminars are planned for the next quarter
 - seminar on hog breeding for the association in Badljevina
 - seminars for sheep and goat breeders on parasite control
 - seminar on mastitis and somatic cells for dairy farmers
 - seminar on Cooperative Advantages in Grubišno Polje

FLAG Petrinja/Former Sector North

Quarterly Report

1 July – 30 September 1999

I Significant Events

Mr Alan Chelko resigned from his position as Regional Director for FLAG Petrinja. On October 1, his position was assumed by Mr David Zuric. Prior to working with FLAG, David worked for more than 25 years in sales, marketing, and international trade in Croatia, Australia, and Taiwan. He has also created and managed a private start-up company in Croatia and knows the ins and outs of the challenges facing SMEs in Croatia. David graduated from the Hotel Management Educational center in Zagreb and attended the University of Zagreb's Economic Studies program. He completed a focus marketing and business course in Australia.

The FLAG Petrinja outreach program included the following events:

The Petrinja Team appeared on a TV news program featuring an interview with FLAG volunteer James "Skip" Meneely who was on assignment at KORDUN JSC, a FLAG Petrinja client in Karlovac. The segment lasted about two minutes and included general information about FLAG Croatia.

VE Gene Hodgkins was instrumental in the organization of 5 farmers associations and, during his stay, conducted daily meetings assisted by FLAG's agricultural advisor Tihomir Gorsa.

VE William Lord gave a seminar to the Beekeepers Associations in Sisak and visited a number of beekeepers on their premises. His seminar had very good attendance with around 50 people present.

On September 9, FLAG Petrinja sponsored a "Big Ag Meeting" on the premises of the Gavrilovic canteen. The seminar was attended by approximately 120 guests, mostly farmer association members from all over Croatia. The seminar also included the leaders and deputies from the Union Of Coops, numerous agricultural companies, marketers, and a great number of NGOs. Chief Of Party Mr Mark Grubb delivered a speech on FLAG efforts to help construct a policy platform for reform in agriculture. The opening statement was delivered by Mr Gjuro Gavrilovic in which FLAG was praised as a cooperator and benefactor assisting Gavrilovic Ltd in reaching its potential supply market, making technological links, and making available Mr Fred Billerbeck, a VE on HACCP standardization.

David Zuric accompanied VE Jim Rathbun to a roundtable discussion about industrial relations with Dok-ing, Kordun, Rukotvorine, and SEAF.

II Business Highlights

Overview

VAT seems to be the main obstacle in SMEs' cash flow. The fact that businesses have to pay 22% VAT to the government immediately after invoicing clients instead of after collecting receivables has been causing the general business slowdown in the Sisacko-Moslavacka and Karlovacka regions (as well as throughout Croatia). The lack of affordable credits means that

the entrepreneurs cannot finance the delayed payments for their goods. Several companies with excellent products, which are competitive on the export market, have been brought close to bankruptcy. These still represent a prey to “would-be tycoons” offering deals with banks which they cannot honor, in exchange for majority shares. Other recently privatized companies have been laying low, shielding their marketing activities from the public in order to protect their numerous small shareholders’ shares from attracting the attention of these “tycoons”. The takeovers practiced in the past by buying small shareholders shares out at grossly discounted value seem to still cause fear in some companies’ management teams.

Links in supplies and sales have suffered due to the huge national internal debt (K27 billion) and the new foreign markets are hardly reachable because of manufacturers’ inability to finance raw materials, technology, and running & fixed costs.

There is an urgent need for a strong SME lobby. The Croatian Employers Association (HUP) has been offering support to only a few big business interests. The newly formed SMEA (Small & Medium Entrepreneurs Association) can only claim 25 signed members. At present, SMEA also lacks effective management, resources, and strategies. On the other hand, if consensus could be reached among syndicates, SMEs, the Coop Union, agricultural associations, and small business and farm interest groups, a strong voice could be raised to influence government policy makers through specific demands.

There is a need for better distribution of information through the business community. Seminars by professionals from overseas (like the WORLD LEARNING-TRANSIT ICT seminar on agricultural policy reform recently held in Zagorje) could be held to educate business leaders on ways of jointly lobbying the government. A challenge to domestic businesses is posed by a strong pro-imports lobby with ties to representatives of the governing party in the Croatian Parliament.

The government itself has not shown any regional development strategies, especially obvious in the former UN sectors. Parts of these areas now resemble “forgotten land,” controlled by arbitrary county executives. Legal advisory and administrative bodies show animosity towards offering good service to the entrepreneurs. The few local municipality leaders who are interested in more progressive policies are hindered by the counties’ written and unwritten centralized policies. The heavy mine contamination around the borders of the Sector North act as deterrent to any outside investors.

The town of Vojnić has three industrial companies that have been struggling against the odds. There is an initiative from Kaplast JSC, FLAG client and a success story, to recruit technological partners for waste PET and plastics recycling nationwide. Petrinja is awaiting Gavrilovic Ltd to start a slaughterhouse which will provide spillover effects to other local SMEs. Although Gavrilovic Ltd belongs to the larger size producer group and is not a signed FLAG client, it is cooperative with FLAG -Petrinja and is the backbone of the business community. They have shown profit without taking on domestic or foreign debt. Karlovac Municipality has a great number of small businesses which are working to overcome challenges, but they are unsupported by the local bank, Karlovačka Banka.

Some of FLAG’s industrial clients suffered consequences of the NATO bombing campaign as they are heavily dependent on orders from the tourist industry, which was deeply affected by the military action.

Clients

This quarter FLAG Petrinja continued to support its 8 business clients and adopted 1 new one

Dok-ing Zagreb based de-mining equipment producer and mine removal company Dok-ing employment stayed steady at 22 full time workers and 4 subcontractors Revenues were \$357,000 for the quarter The outstanding receivables are \$572,000, with most carrying over from the previous periods The main three debtors are Mungos, RuRu, and the Israeli company Maverin Dok-ing is currently producing the MV2 Earth Angel de-mining vehicle for CROMAC, (Croatian Mine Action Center) Financing was obtained from Zagrebacka Banka (\$60,000) Dok-ing capacities for de-mining are now at 1,000,000 per month with 3 MV2s operational Since clearing its arrears with SEAF in June, Dok-ing is now preparing to request another loan from SEAF to build the larger MV3 Dok-ing hopes to attract U S investment for de-mining jobs in the Balkans, being in an advantageous position as a SEAF equity partner, FLAG client, and with a transparent business operation

KaDrvo Producer of beechwood elements in Vojnic This company has kept its 48 employees and continued to export its mid to high quality European standard product used mainly for house stairs The firm is threatened by lack of working capital and the creditor Karlovacka Banka The managers have signed over control of the company to Roman Reicher of ISADE – FITRACO Holding, believing that more funding and favorable repayment terms would be negotiated However, FLAG is reviewing the status of KaDrvo as a client as there has been no movement from the new manager and an extension has been requested for the takeover contract

Kaplast Eko Plastic injection molding producer of beverage cases and electronic components in Vojnic The firm is continuing its strong performance with gross turnover of \$1,943,000, receivables of \$526,000, and 63 employees (13% increase in employment) Kaplast Eko is negotiating support from Ecolinks for PET and national waste plastic recycling The first reaction from Ecolinks was rejection on the basis that waste plastics were not Kaplast's problem but the problem of the county or the whole state FLAG, Kaplast, and Ecolink's Sandra Balent are researching ways of bringing the project into the Ecolinks framework FLAG has also started the search for a foreign or domestic technological waste plastic collection partner This business is normally one of the most lucrative ones and the proposal from Kaplast is economically attractive

Ferro Art Biscan Petrinja based producer of wrought iron products such as fences, gates, window bars, and spiral staircases This trade shop has been progressing with acquiring new loan approval from Caritas bank through Zagrebacka Banka for \$12,000 in working capital It is also anticipating a second meeting with SEAF Mr Perica Biscan, the proprietor, has been engaged in buying machinery and other equipment from Germany He is awaiting arrival of equipment and materials, after which he is to start his first commercial contracts F A has had no revenues and no receivables

Rukotvorine Family run handicraft maker in Petrinja They are still concentrating on making insignia ceramics for different businesses, hotel chains etc FLAG continues supporting Rukotvorine by linking them with credit information and cash customers The existing receivables are \$4,300 from the last tourist season

TIM Topusko based producer of stretched metal fencing and construction props The company delivered 118km of highway railing to the Bechtel project Bregana-Zagreb The complicated shareholder situation remains (more than 300 shareholders) while FLAG continues to support

TIM's marketing efforts in Bosnia-Herzegovina The firm is trying to settle key shareholder issues before committing to dates for a visiting volunteer

Silikem The start of production is still delayed because of the majority owner SAMOBORKA's commitment to its \$12,000,000 reconstruction and modernization project in Samobor FLAG brought SEAF for an evaluation visit and is continuing efforts to locating an independent source of immediate working capital for Silikem Once the production begins, FLAG will bring an expert volunteer to help the company streamline its production and processes Silikem has expressed interest in the marketing assistance from FLAG once the ceramic tiles are in production

Staklo Prom Staklo's main concern is to secure credits and find more paid work The situation has improved since the last quarter, and a new employee has been added FLAG has made links for Staklo with Gavrilovic Ltd re window reconstruction on Gavrilovic building This project is still pending

New Clients

Kordun JSC Signed industrial stainless steel products company with 420 employees, signed in the RAP municipality of Karlovac VE James Meneely (former president of Armco Steel) worked seven weeks with the company, analyzing marketing, production and general management He recommended reorganization of sales strategy, production, and general and financial management An industrial engineering VE may be requested if the company carries out VE Meneely's recommendations

III Agriculture Highlights

Overview

The agricultural sector is experiencing challenges similar to that of other war-affected areas of Croatia Typical challenges are damaged or destroyed infrastructure, lack of able personnel, low land value, and lack of credit Production methods are outdated and need to be brought up to standard with foreign competitors Local markets provide minimal outlets for local goods Local producers are suspicious of receiving help from NGOs, and current middlemen attempt to convince producers to deal only with them

The Sisacko-Moslavacka and Karlovacka regions are potential large livestock producers Sisacko-Moslavacka is suited for hog, cattle, and horse farming while the land of Karlovacka lends itself to sheep farming Modest numbers of livestock have been reintroduced by local producers FLAG has been making efforts to organize them into associations with the aim to make substantive links with meat and processors such as Gavrilovic, Krizevcanka, Dukat, and others FLAG has been cooperating closely with both counties local agricultural extension programs and have sent the counties' advisors and association leaders to the US on a TRANSIT program In addition, FLAG is working on market research for organic food, enlarging herds of cattle, and trying to establish an association presence at one of the local savings and credit unions

Clients

Tremusnjak Association (Petrinja) 24 members (23 Serbs, 1 Croat)

They are currently engaged in repair of infrastructure, electricity, road, telephones

Susnjar Association (Petrinja) 14 employees (all Serb)/ They have started the cooperative for cattle, currently fattening 100 They are also engaged in repair of the road and the telephone

Plod Zemlje Association 26 members (24 Croats 2 Serbs) They have initiated cooperative relations with Veterinary Station –Petrinja

Bobovac Association 20 members (17 Croats, 3 Serbs) They are concentrating on free grazing cattle production and currently have 500 calves of 300kg FLAG has made efforts with Gavrilovic and abroad to invite potential long term buyers

Budicina Association 14 members (all Croats) They are engaged in reconstruction of their village FLAG has assisted CCI to enter the village with their social assistance program

Bijelnik Association 23 members (22 Serbs, 1 Croat) Currently cooperating with OSCE and British Know How Fund The Know How fund is offering to finance a tractor and equipment purchase FLAG has been coordinating letter of intent from Gavrilovic, and IOM and OSCE recommendations The association is also engaged with the village reconstruction, including waterworks and telephone

Banski Grabovac Association Grabovac is repairing infrastructure, telephone, etc FLAG assisted in bringing a CCI civil initiative training program There is a plan for renovation of the social premises to be used by the association

Krnjak Association Their registration is in processing FLAG has designed a questionnaire for the members and is organizing channels for distribution of information

Donja Stupnica Association The registration is in processing FLAG has designed a questionnaire for the members and is organizing channels for distribution of information

AGROZRIN Agrozrin continued cooperation with Mr Mihaljevic, a SEAF client from Vrbovsko, to gather native products such as snails The firms now collects mushrooms in Dvor municipality There are 9 buy-off places in different villages and one buy-off station in Dvor There are more than 50 people involved in gathering and the result of a workday varies between 350 kg and 600 kg There is a competition in the region and the buy-off price changes from day to day It was 15 HRK and now is only 10HRK per kg Agrozrin has earned about 35,000 HRK gross dealing with Mr Mihaljevic Also, about 100 villagers earned more than 100,000 HRK for collecting wild mushrooms

Events

- FLAG visited the Zagreb Autumn International Fair which proved one of the best ways to identify marketing links for agricultural products Talks were held with DARbo, Kandisin, Zlatni Vrtovi, Garden Land, Krizevcanka, Segestica, Chantelle, Familia, Iprom, AssiDomain, Ekos, Olma, Krizevcanka, Stanic, Zvecevo, Koestlin, Jakpoc, Puris, Inter Agro, etc

- FLAG –Petrinja made an appointment with Mr Ivan Kolar, the leader of the Farmers Association Of Croatia, (30,000 members) This is the same organization that had organized the farmer’s protests in June this year regarding government unpaid dues Mr Kolar and FLAG agreed on issues detrimental to current agricultural production A decision for next was made to invite other organizations such as the Croatian Union Of Coops, Independent Ag Syndicates, Union Of Farmers Of Slavonia and Baranja, SMEA, Croatian Fruit Growers, Croatian Milk Processors Association, Croatian Meat Association, and others
- Alan Chelko, Gene Hodgkins and Dave Zuric visited Gavrilovic to talk with Mr Stoic about the Meat Processors Association contribution to the roundtable discussions regarding a consensus for agricultural reform Hrvatski Stocar, an umbrella association of stock producers and stock product processors, was recommended by Mr Stoic to be brought into the discussion about agricultural reform
- FLAG representatives were also present at the Final Report meeting at Gavrilovic by VE MR Billerbeck and were present at the meeting between Gavrilovic heads, ESCO managers, and SFOR people FLAG emphasized the possibility for Gavrilovic and local farmers as potential suppliers to SFOR, and was strongly supported by VE Fred Billerbeck Gavrilovic also expressed strong interest in helping FLAG link to them to Kosovo sales of Gavrilovic canned and vacuum packed products
- FLAG representatives together with Mr Billerbeck and Mr and Mrs Stojic visited the Park of Nature Lonjsko Polje The hosts, Mr Anusic and Mr Misic made a presentation of the respective natural resources and informed about pastured pigs from Lonjsko Polje Gavrilovic is interested to buy 100 grown pigs for processing purposes as a pilot production project
- Alan Chelko and Dave Zuric (together with reps From other FLAG offices) met with CDC representative Mr William W Elfenbein They were briefed on the importance of FLAG’s inputs into CDC database regarding FLAG clients who are interested and ready to supply basic staples and commodities to Kosovo CDC had the funds prepared and FLAG was urged to expedite information processing Six weeks have passed, FLAG has entered a large amount of data into the system CDC has not given any feedback to FLAG or its clients

IV Upcoming Events

- FLAG Petrinja will continue to identify SMEs having the potential to impact the return process with technical assistance FLAG Petrinja is engaging in assistance to SMEA and its business plan development
- VIVERA Ltd Glina Upon approval from Osijek, Petrinja will sign MOU with them regarding technical and marketing BAC assistance Since Vivera might find itself on the market for takeover, FLAG will make contacts with US food producing companies to research their interest in buying Vivera
- Pčelarstvo KEP honey packaging operation with 1 full-time and 1 part-time employee The BAC has identified this company as having a good potential for developing beekeeping in the area, per VE William Lord’s advice

- Grating Ltd Karlovac, FLAG intends to conduct diagnostics and investigate further into possibilities of MOU This industrial chemical company is a potential SEAF investment Management is negotiating a stone quarry concession in Lika area nearby an important Bechtel highway and tunnel junction
- FLAG Petrinja is currently working with a farmer group in the process of creating an association Assistance includes organizing the first meeting and preparing registration paperwork In the coming months, we anticipate forming the following association
 - Donji Vidusevac hog breeders association with all professional members, formerly cooperating with PPK and Gavrilovic
- FLAG Petrinja intends to organize the following

Research of the technologies of production of the chestnut flour mills for the Sisacko-Moslavacka region for supplies to LED, other food companies, and the pharmaceutical industry The Sisacko-Moslavacka region is abundant in chestnuts and FLAG client Agrozn's work-plan includes chestnut collection At this stage Croatia imports chestnut flour in the range of 300-400T per year

- The following seminars are planned for the next quarter
 - Marketing seminar for FLAG SME clients in Sisacko-Moslavacka and Karlovacka regions conducted by professor Hitrec, the honorary lecturer at the University of Economics and one of the founders of SMEA The seminar's main them will be standardization of domestic products towards the foreign markets and systemization of the domestic & foreign marketing ways

In cooperation with FLAG Daruvar, FLAG Petrinja will organize and participate in

- seminar on hog breeding for the association in Petrinja
- seminar on mastitis and somatic cells for dairy farmers
- seminar on Cooperative Advantages in Petrinja
- Dani Meda in Daruvar

FLAG Knin / Former Sector South
Quarterly Report
1 July – 30 September 1999

I Significant Events

- FLAG Knin formed the multiethnic Sheep-Breeders' Association of Korenica, organizing the foundation assembly meeting and administratively registering the association. This association has over 40 members who own over 2,000 sheep.
- FLAG Knin signed an MOU with one new business client, one new agricultural association, and one new agribusiness client during the quarter.
- FLAG Knin developed a project to purchase sheep for returnees on a rotating-fund payback basis in Obrovac. However, municipal hostility to the project necessitated a switch to the Udbina municipality. The increased price of the sheep due to the delay in executing the project in the end resulted in its postponement, but nevertheless the knowledge and research is there to activate this project on a regional basis as funds become available.
- FLAG organized radio advertisements (on Radio Gospić) for sheep farmers to organize in the Korenica area. These advertisements outlined the benefits of association forming and contributed to the high turnout at the formation meeting.
- Damir Buntić joined the FLAG Knin staff as the Agricultural Advisor. His main duties have been providing assistance and advice to returnee and other farmers in the area and encouraging association/cooperative formation. He has a degree in Agriculture from the Agricultural Faculty in Novi Sad and was previously employed at the UN base in Pleso.
- FLAG Knin provided a computer program on optimal feed mixtures to a feed producer in Labin which will enable him to create the optimal feed mixtures based on customer requirements, making him more competitive in a difficult market environment.
- FLAG Knin completed two volunteer assignments during the quarter and provided assistance to six business clients and four agricultural clients.
- FLAG Knin sent four of the local Agricultural Extension Agents active in our area to attend TRANSIT (World Learning) training in the US for three weeks in August. They returned with solid ideas about improving agriculture in their area and are working with FLAG to realize their plans.
- FLAG Knin provided guidance to the municipality of Biskupija that assisted them in solving a problem with an IOM-funded water project.

II Business Highlights

The economic environment for SMEs in this area is still very difficult. Lack of access to credit, lack of liquidity, over-regulation, and absence of any credible support to small businesses are substantial hurdles to SME growth. An aggressive and antagonistic financial police administration penalizes small business owners for the smallest infractions, and inspections and

cumbersome record-keeping requirements reduce initiative and productivity Most of our clients are focused more on survival than on expansion

This quarter FLAG Knin supported the following six business clients

Tomaic-commerce (new client) Cheese producer from Krasno near Otočac They produce cow and sheep cheese Mr Tomaic will buy all sheep milk produced in the area from members of the **Sheep Breeders' Association of Korenica**, which was organized by FLAG Through this linkage FLAG will help the cheese factory increase production, sales and revenues and also help farmers in the area increase their income through the sale of milk VE McNeil also provided advice that will help them increase production

Ribarstvo JSC Fish farm based in Donja Suvaja at the spring of the Una river They farm exclusively rainbow trout, and unusual to Croatian trout farming methods, Ribarstvo has its own hatchery FLAG established a linkage between Ribarstvo and a small fish farm in Zagreb This fishery started to buy fingerlings from our client We also created a link between our client and a local fish trader who became the major distributor of fish in the Knin area This year the fishery is operating for the first time at its full capacity of 100 tons of trout per year Aside from having trouble collecting receivables, a major problem was getting the proper food at the right time FLAG helped them contact Dutch and Danish suppliers who will provide them with a reliable source of fish food Projected revenue for this year will be more than double the previous year's revenues of \$128,000

Građevinski obrt Petar Rajčević Contractor from Donji Lapac who is working on the reconstruction of the Donji Lapac area Mr Rajčević is also the owner of the only store for building supplies in Donji Lapac We provided him information about tenders for rebuilding in the region After getting ICMC donations and with new equipment, he will be able to bid independently for bigger projects Mr Rajčević has succeeded in maintaining contracts and revenues at the same previous level of \$22,000 per quarter

Concurent BIS Seed potato producer from Udbina With over 150 hectares of land they organized production of not only seed potatoes but also different kind of vegetables mercantile potatoes, onion, cabbage and lettuce Because of seasonal business cycle during the summer and the fall they have no revenues, their major revenues are realized from November until March FLAG intends to help them in linking with bigger suppliers of seed potatoes

Oštra Producer of powdered beverages from Udbina The owner is a returnee from Canada and his partner is still in Canada Oštra can produce instant coffee and other beverages with brand mark as required Oštra also packs sugar in small bags with their label To resolve liquidity problems they recently opened a second retail store in Udbina to sell goods which they get from customers instead of their cash receivables

Vrana dairy Dairy farm managed by Mrs Blanka Mitrovic The dairy is one of the main milk producers in Zadar county A FLAG VE made a linkage with a supplier of milking equipment in the U S because the current milking facility was not suitable for milking Mrs Mitrovic is now very satisfied with the results We also assisted them this quarter with a contact in the U S who provided free testing of samples of their soil

III Agricultural Highlights

With the almost complete absence of a manufacturing industry in the former Sector South (except for some now-defunct former state enterprises), agriculture will be key in the development of an economic base that will encourage refugee returns. The best potential for income generation and refugee return in relatively depopulated Northern Dalmatia is through the conversion of grass into meat and milk. Although the meat market is strong, the collection and sale of milk in this area is considered economically unsound due to the distances between the producers and a dairy, the expense of transport, the absence of milk-cooling units, etc. Wool is also not collected due to lack of information about markets and transport difficulties. We believe that these difficulties can be overcome through the organization of existing producers to achieve economies of scale and cost pooling, and we are actively engaged in this effort.

FLAG Knin held the foundation meeting in Korenica of the **Sheep-breeder's Association of Korenica** last month. There are a total of 40 members who collectively own over 2,000 sheep. The ethnic mix of this association is approximately 50-50. This association will foster the reintegration process by providing a vehicle for members of both ethnic groups to interact and exchange information. The return issue will be developed as Serbs who have already returned become economically viable sheep producers, a process which through word of mouth will encourage other refugees to return to Croatia. This is an example of how associations can contribute to population reintegration efforts and we will use this association as a vehicle to implement technical and other assistance to returnee farmers in the area.

With VE assistance, the FLAG Knin agriculture representative has designed a series of seminars on Flock Management, Nutrition, and Disease/Illness Identification. Interest of local producers in learning the optimal methods of raising sheep was high, as was demonstrated at the association formation meeting. These seminars will be key in giving sheep producers the tools they need (knowledge and training) to raise a healthy sheep flock. Over 10 impromptu seminars have been given to small numbers of sheep producers with good results and high enthusiasm.

FLAG Knin is also leveraging a sheep donation being made by the Lutheran World Federation (a local NGO) in the Udbina-Korenica area. Over 1,000 sheep were given on a humanitarian aid basis to 200 families (mostly Serb returnees) to help them survive the winter and/or to provide a small income by selling lambs in the spring. We expanded the scope of this aid into the sphere of increased return/reintegration and economic development. We have used FLAG technical expertise to form an association to expand the market power of each producer and also add to the value of these sheep. Lambs sell at a premium in Croatia and this is an opportunity to turn what are normally subsistence-level returnees into small-scale, profitable sheep producers.

This quarter FLAG Knin supported the following four agricultural clients:

Gučanin (new client) Sheep operation in Udbina. They have been milking their 700 sheep and providing the milk to a cheese producer in Pag, which for the last quarter has been unable to pay due to financial problems. FLAG Knin put them in touch with client **Tomaic-commerce** who will begin buying the milk and paying in cash on delivery, and at a higher price than that of the Pag cheese factory. This will result in an extra \$20,000 next year for Gučanin which they will use to increase the size of their flock.

Sheep Breeder's Association of Korenica (new client) FLAG organized this association to increase the bargaining and marketing power of these 40 producers and to assist them in developing value-added processes (milk and wool production) for their sheep. We have put them in contact with textile firm **Regeneracija** north of Zagreb who will purchase all the wool this association can provide. We are also negotiating with **Tomaic-commerce** to arrange milk

sales to his cheese operation. These contacts will result in increased income for these members from milk and wool resources that until now have been thrown away.

Perak Mr Ante Perak is one of the biggest sheep breeders in the area of Bribinske Mostine. He has a flock of approximately 1,000 sheep and goats and is planning on forming the only sheep reproduction center in Northern Dalmatia. He had problems selling his lambs so FLAG recommended that he roast the lambs by himself and then sell the prepared meat to tourists. In this way he sold most of his lambs and earned a great deal of income since he sold one kilo of lamb for less than the usual price in restaurants, but much higher than the price he usually receives for selling live stock.

Peraic d o o Mr Peraic is a fruit and vegetable producer and retailer. He plans on building a large facility for packing fruits and vegetables. He has not yet found the necessary financing for this project. FLAG assisted him in applying for several types of credit and loans and we are still waiting for a response.

IV Upcoming Events

FLAG Knin has the following activities planned for the next quarter:

- FLAG Knin will begin evaluating economic opportunities that will facilitate the return process. These opportunities may include providing limited funding for income and return-generating activities that deal mainly with agriculture.
- FLAG will continue to organize sheep producers and other farmers into associations, focusing on the return-friendly municipalities of Donji Lapac, Otočac and Biskupija.
- FLAG will continue to identify SMEs with which we can facilitate the return process by providing technical and other assistance.
- FLAG will actively search for ways in which resources can be leveraged with those of other NGOs, primarily IOM, CRS and ICMC, to increase their impact.
- FLAG will organize the milk producers in the area south of Knin into an association to assist them with selling their milk, in exchange for cash on delivery, to a potential client in Pakovo Selo who has a dairy and will produce specialty cheeses and yogurts.
- FLAG will use the expertise and enthusiasm of our four TRANSIT participants to form new associations and facilitate population reintegration. We are actively engaged in a project with the agriculture extension agents in the Otočac area to increase farm production.
- In cooperation with IOM Knin and a local consultant, we will attempt to organize a cow milk collection operation in Donji Lapac. This will give returnees in this former 95% Serb RAP municipality a source of income which they do not currently have.

FLAG MONTENEGRO 4th QUARTER REPORT

1 July—30 September 1999

The original proposal for Montenegro provided for one American, initially stationed in Dubrovnik, three local nationals and eight volunteer assignments. The initial focus was assisting specific large state-owned firms to adjust to a market economy with a longer-term goal of restructuring to facilitate privatization. We were also asked to look at opportunities for cross-border trade.

FLAG Montenegro opened its office in Podgorica on 21 July and currently operates with two expatriates and three local nationals. Major activities to date include

OBOD The assessment provided at the Montenegrin Economic Working Group in Cavtat underscored the challenges faced by this state-owned firm. OBOD demonstrated all the deficiencies associated with a command economy: redundant workers, lack of accountability, poor management, no marketing, reliance on compensation, and poor maintenance. FLAG stated that business criteria would dictate closing the firm. Political considerations necessitated that OBOD be put on life support and an attempt made to restart production. It was judged that closing a factory with 2500 workers in the pivotal city of Cetinje would destabilize the government. The challenges facing OBOD are onerous, but progress has been made. Carl Moe, FLAG consultant to OBOD and recently retired president of Maytag International, initially felt the probability of success was less than 20%. Based on his recent visit he now feels it is greater than 70%. Most of the uncertainty involves the government's ability to arrange financing for working capital and severance for excess workers.

The fifteen weeks of volunteer/consultant effort in the first quarter have produced tangible results. In part because of our recommendation a new general director has been appointed. FLAG developed a comprehensive action plan to return OBOD to production as a "for profit" enterprise. This plan was adopted by the Board of Governors and gained the support of the government. FLAG brokered an agreement between the government and the head of the unions for Montenegro to assure labor peace.

Efforts continue and we hope that the U.S. Government's promise to support a management team for OBOD and provide working capital will be honored.

Niksic Steel This company shares many of the same characteristics of OBOD. Unfortunately, the company produces a commodity at a price significantly higher than the world market price. Moreover, current management seems unwilling to face the realities of the situation. FLAG outlined five specific actions that required no funding as a precursor to restarting production. FLAG assisted the government in selling approximately 7,000 tons of old inventory which resulted in earnings of about 1.5 million dollars. FLAG has limited its activities at Niksic due to resource constraints, the government's priority towards OBOD, and management's lack of cooperation. We have offered, through the Ministry of Industry, our financial consultant to Niksic to help them capture costs so they can make management decisions.

Wood Industries FLAG evaluated two large wood producers in the North of Montenegro. We provided specific recommendations that would make them more competitive selling to international organizations in Kosovo. We provided several NGO contacts, one of which resulted in a 1.5 million DM contract.

Cross Border Trade FLAG negotiated a contract funded by USAID/ OTI for a survey of 250 large firms representative of the Montenegro economy. It provided a database that indicates how closely the economy is tied to Serbia and the surrounding states. It indicates cross border trade opportunities and it formed a basis for CDC efforts to provide supply side information for Kosovo activities.

Tourism Industry FLAG conducted a comprehensive study of the tourism industry in Montenegro. After discussions with the Minister of Tourism in Cavtat, Ambassador Sklar asked if FLAG could provide this activity. The study provided specific recommendations, including modification of Montenegro's approach to hotel privatization. As a result of our suggestions, the Privatization Council decided to offer management contracts for about 15 hotels to international chains.

KAP Although concerned about the sensitivity of Glencore's management contract with KAP and the government's avowed approval of Glencore, FLAG has an experienced consultant standing by to evaluate the operation.

Privatization and Other Issues

Montenegro is committed to move quickly with three programs—mass voucher, international tenders, and auctions. Officials repeatedly stress the need for speed and transparency. Our concern is that merely transferring the assets (and liabilities) will not produce the investment needed or the management required for meaningful change. Success with privatization is linked with effective supporting policies and effective institutions that foster private enterprise. With Barents' ability to deploy assets in Montenegro constrained, we had been asked to investigate possible assistance.

Montenegro's first priority is a stable currency and policies regarding establishment of a currency board and a convertible dinar are being investigated. Professor Vukotic, President Djukanovic's chief economic advisor, requested FLAG assistance in the banking sector. Our consultant met with several key players interested in banking reform and we expect his report by 20 October. Public trust in commercial banks is practically non-existent, and capital that can assist SME development is unavailable. Restoring confidence in the banking system is essential to attracting investment and the eventual success of the privatization process.

There are few alternatives to entrepreneurs who require capital to expand their operations or to develop new opportunities. Opportunity International's success with their micro-credit lending program covers only a small segment of the market. Larger enterprises will need some type of loan facility to meet their needs.

Privatization, SME development, and banking reform are interconnected in Montenegro. In addition to legal and regulatory reform, development of capital markets are also required so that the privatization process does not become an end in itself.

Attachment A Table of Clients in RAP and/or PRM municipalities

Company and Association Clients	Legal_Form	City	RAP	PRM
Ferro-Art Biscan	Ltd	Petrinja	Yes	No
Construction craft Petar Rajčević	Craft	Donji Lapac	Yes	Yes
KaDrvo	d o o	Vojnić	Yes	Yes
Kordun	JSC	Karlovac	Yes	No
Nešić- Bijelo Brdo	Ltd	Bijelo brdo	Yes	No
PZ 'Vocko'	Coop	Prekopakra	Yes	No
Rukotvorine Petrinja	Craft	Petrinja	Yes	No
Samtex	Craft	Gaj	Yes	No
Staklo Prom	Craft	Petrinja	Yes	No
Stočarsko-svinjogojska udruga	Assn	Badljevnina	Yes	No
T I M Tvornica Istegnutih Metala	Ltd	Topusko	Yes	Yes
U P Bjelnik	Assn	Blinjski kut	Yes	No
U P "Tremusnjak"	Assn	Jabukovac	Yes	No
U P "Budicina"	Assn	Petrinja	Yes	No
U P "Susnjar"	Assn	Jabukovac	Yes	No
Assn Plod-Zemlje	Assn	Jabukovac	Yes	No
Peasant assn Bobovac	Assn	Bobovac	No	Yes
Usluga	Ltd	Pakrac	Yes	No
Werba	Ltd	Osijek	Yes	No
Zajednica Udruga Seljaka Slavonije i Baranje	Assn	Osijek	Yes	No

Small and Medium Business Enterprises Policy Resolutions September 1999

PREAMBLE

The promotion of private enterprise in our society provides for economic opportunity to all sectors of the population. Economic growth and stability can only be achieved with a strong environment for entrepreneurs and the start up of small and medium businesses. We are dedicated to advocating for more favorable conditions for business, thereby strengthening our economy and fostering commerce. We further recognize that current economic conditions require the positive actions of government in finding acceptable resolutions to the problems that we face. We will work with our government to create an environment, which allows for the creation and nurturing of small and medium business enterprises. We will also assist the government in programs that will foster an open economy and create jobs, allowing for economic freedom for all.

Petitioning one's government is the mark of a free and democratic society. Businesses, associations, and government officials united together for a common goal of promoting a more favorable business climate is the solution that we seek.

Economic Policy for Small and Medium Business Enterprises

The foundation of a sound economy are the Small and Medium Business Enterprises. The primary objective of a national economic policy must be to maintain the economic viability of SME's. This policy should also seek to enhance business income and production, so that business may continue to employ people and produce needed goods and services.

Payments to Small and Medium Business Enterprises - The biggest problem facing SME's in Croatia is the government's practice of delaying payment for the services for which it has contracted. This has caused a ripple effect in the economy, leading to inadequate cash flow and even insolvency among many SME's. The highest priority of the government should be to pay business within a reasonable time period and at the contracted price or to ease the tax liabilities of business during this extended period.

Taxation of Business

The Croatian government has used the excessive taxation of business as a means of sustaining an ever-growing budget. These taxes have become burdensome and tremendously regressive to SME's and ultimately to the consumer. Taxation has hindered business's ability to export to the world market and to compete with cheaper imports. This excessive taxation has led to a large black, and gray market, denying government any revenue. The government must take steps to

reduce the tax burden to SME's, thereby stimulating economic growth and increasing tax revenue

Value Added Tax Adjustment – The foundation of the Croatian economy is its small and medium businesses. The production of goods and services as well as retailing is functioning under a burdensome tax system. The government should allow for a graduated VAT for varying product sectors. Many of the competing countries have a graduated tax rate for varying products and services. A proposal for a multi-level VAT would allow for basic essentials to be charged no tax or at the least rate, raw materials used in production would be charged a competitive rate, and luxury goods charged at the full rate.

Tax Remittance – In order for business to maintain a positive cash flow thereby stimulating the economy, the government should allow for a longer period for remittance of the Value Added Tax. At present, the VAT must be paid in the month following invoicing. Because of this, many businesses have a cash shortage while awaiting payment. This increases the need for short-term capital or delays the payment of other liabilities. The system of collecting the VAT should be changed to allow for remittance upon the receipt of payment. Another solution used in many competing countries is to allow for remittance of taxes every quarter or semiannually.

Taxation of Payroll – Unemployment is an issue that is hampering economic prosperity in Croatia. The government should take steps to reduce the payroll tax burden in order to stimulate employment. Government could also make attempts to work with business start-ups and entrepreneurs to enhance employment opportunities through the use of the Croatian Employment Services' program for subsidized employment.

Access to Available Credit

Credit - The government's liquidity problem, and a lack of capital in domestic banks, has produced credit problems for SME's. Too often credit is not readily accessible to SME's and when available the terms are excessive. Many of the loans obtained by SME's have terms at above market interest rates, for short terms, and with excessive collateral. Measures should be instituted to allow for the availability of credit at market terms and administered in a fair, prompt and transparent manner. The government should also allow for more usage of the Croatian Guaranty Fund for reduced collateral on loans.

Some governments in the war-affected areas, through a national credit program, are attempting to loan money at a reduced rate (9.8 percent), however many of the counties and/or municipalities have not lent this money in a consistent manner. In order to promote the start up of business enterprises, the government should mandate that this money be loaned to entrepreneurs in a timely manner and with minimal collateral.

Enterprise Zones - The government through a comprehensive program in the war-affected areas should create an environment for the start-up and growth of SME's. This could be accomplished on the municipal or county level, with assistance from the national government. One such program was instituted in the town of Pakrac (see attachment 1). The Pakrac Industrial Zone program could be used as a model for other municipalities and counties. This model program uses the property of a former state owned industry, which is insolvent. SME's will be allowed to purchase needed space at a reduced price with all needed infrastructures in

place It will offer favorable terms on credit, consulting services, subsidies for employing and educating workers, duty free imports, and tax benefits to the employer

Pro-Business Advocacy

Advocating ones position before the government is the right of all citizens in a free and open society SME's, business associations, unions and other organizations should coalesce to advocate the position of businesses in Croatia The goal of business should be to identify operational issues that would allow for reasonable successes and work with government on solutions to the policies and regulations impacting the business climate in Croatia Government should also seek the input of business associations, SME's and other organizations in their formulation of legislation

Attachment C Agriculture Policy Resolutions

Agriculture Policy Resolutions July 1999

PREAMBLE

The private farm system of agricultural production can provide opportunities for individual enterprise to all families in our society. This system achieves economic and social stability, as well as soil, water and environmental stewardship of our natural resources and unparalleled production efficiency. We are dedicated to the strengthening of farmer cooperatives and privately held agribusiness's and farms. We further recognize that current conditions require strong government involvement in resolving problems. We seek to work with the government in creating conditions where free market principles guide the destiny of Croatian agriculture and government involvement is that of facilitation and to provide a safety net in times of unforeseen circumstances.

The essence of the cooperative movement—farmers working together for their mutual benefit—is the spirit, which motivates every activity of the Slavonia-Baranja Farmers Union. Private farmers have a valuable tool in working together in farmer-owned-and-controlled cooperatives. These cooperatives are essential to the farmer's economic well being and success.

Agricultural Programs for Private Farmer

National Food Policy

The keystone of a free, progressive, democratic national society, as well as a strong rural Croatia, is the owner-operated private farm. The primary objectives of national agricultural policy must be to maintain the economic viability of family-size farmers, and to enhance producer income, so that farmers may continue to provide a reliable supply of food and fiber and serve as stewards of our nation's resources.

The basic issue facing this nation is the control of agriculture. National farm policy must provide direction and emphasis to ensure that control of agriculture is vested within the private farmer. Profitability must return to the rural and agricultural economy. Farmers and consumers alike need stability and fairness in a farm program. Adequate and affordable food is one of the most important security issues that Croatia faces in the future.

Agriculture Payments to Farmers – Croatian farmers are at economic risk because current government policies hinder the flow of inputs and credit needed for agricultural production. It should be the highest priority for the Croatian government to pay farmers within a reasonable time period and at the price promised prior to planting.

Domestic Fertilizer Supply – It is imperative that the agricultural sector has access to reliable and secure supplies of fertilizer. Applications are time sensitive, and yield reductions can be dramatic if rates are curtailed significantly. Adequate domestic production and the ability to import fertilizer are critical to maintaining domestic food supply for Croatia.

Inputs for Agricultural Production – Croatian farmers must be assured adequate inputs for the production of food. Efficient agricultural production requires sufficient quantities of petroleum, farm equipment and machinery, feed and fertilizer, crop-protection tools and general farm supplies.

We support national programs and policies that will encourage production, distribution, and availability of those vital farm inputs through the private sector, including development of improved technologies.

Domestic Dairy Policy – Because Croatia continues to be a milk deficit country, we encourage the Ministry of Agriculture to maintain incentive programs for rebuilding dairy herds. Farmers must also be paid for the milk, which they produce and sell, to private dairy processors. There should be a high-quality, stable supply for consumers with a reasonable profit for producers.

Domestic Livestock Policy – All livestock producers, regardless of size, should have market access and information. Development of farmer-owned cooperatives for marketing and processing presents farmers with the greatest opportunity for economic return.

Livestock Producer Protection Act – We support the creation of a Livestock Producer Protection Agency within the Ministry of Agriculture which ensures timely payment to producers when they sell their livestock to the government or a private business. Each slaughterhouse should post a bond to be in business. This bond will be held in an accredited bank and this guarantees payment in the event of bankruptcy or any payment, which is made later than 30 days after the purchase of the livestock.

Crop Insurance – The Ministry of Agriculture will establish an Office for Risk Management, which will work with the insurance industry and farmers to create an affordable multi-peril crop insurance program.

Commodity Storage Program – Maintaining the quality and condition of a country's grain supply is critical to long term food security. The Ministry of Agriculture should survey grain storage facilities and their proximity to domestic grain production to ensure that adequate storage is available. If adequate grain storage is not available, the Ministry of Agriculture should consider incentive programs, including loans to private farmers, private agribusiness's and cooperatives for the building of grain storage and drying facilities.

Access to Fuel – Agriculture is a very energy intensive industry and needs access to fuel especially during planting and harvesting of the crops. We seek a balanced energy policy, which reverses the trend toward concentration of the ownership or control of sources, production, and distribution of energy. If given the opportunity, farmer cooperatives have an important role to play in the delivery and distribution of gasoline and diesel fuel.

International Trade and Access to World Markets

Croatia has the land and feed resources to be self-sufficient in livestock and poultry production and to be a net exporter. In 1998, Croatia imported 670 million kuna of live animals and livestock products. This large number of imports reduces the price and domestic demand for livestock and lowers net cash income for farmers. Particular notice should be placed on the pricing practices of foreign countries and their impact on the Croatian market.

Imports of Livestock from Subsidizing Countries – The Ministry of Finance should place countervailing duties on products to offset subsidies paid to foreign exporters if there is harm to domestic producers

Imports of Livestock from Non-Subsidizing Countries – Imports from agricultural non-subsidizing countries should be capped at a level that does not disrupt domestic production and markets. The one exception would be a domestic shortage of the product.

Transshipment of Agricultural Products – Many agricultural products enter Croatia to be transshipped to other countries but the products remain in Croatia duty free. The national government must develop a system to track goods that enter Croatia, ensure that the goods leave the country, and assess tariffs and penalties to companies who violate the laws on transshipment of goods.

Country-of-Origin Labeling – It is essential that the consumer has information to make informed choices. All imported meats, fruits, vegetables, foods, dairy products, feeds, grains and fibers must be labeled to disclose country of origin, processor, actual contents and additives.

Imports of Dairy Products – Due to the fact that Croatia is a milk deficit country, a high percentage of fluid milk must be imported to meet the domestic needs of consumers. We encourage the Ministry of Agriculture to closely monitor this milk supply situation so that imports of dairy products do not undercut the growth of the domestic dairy industry.

Farm Cooperatives and the Family Farm

The farmer-owned cooperative is an effective institution through which the farmer can reduce costs of production, maintain a reliable source of inputs, and effectively market and process farm products. A fundamental economic right of farmers is that conferred by national law permitting individual farmers to join together in cooperative associations for the purpose of pricing, processing, marketing and selling their products, and bargaining with processors and handlers for prices and other terms of sale.

Cooperative Services and Law – Government policies should promote and encourage farmer cooperatives to play a larger role in marketing, assembling, processing, merchandising, and exporting farm commodities. The Ministry of Agriculture should take the lead role in facilitating the development of farmer-owned cooperatives. This includes tax policies, which allow capital to be directed toward facilities. It is also important that cooperatives are able to receive financing at a fair rate of interest.

An Office for Cooperative Services should be created within the Ministry of Agriculture, which works directly with farmers in the organization, and development of cooperatives. To be successful, cooperative development in rural Croatia needs better access to capital, markets, and expertise. The Office of Cooperative Services needs to be structured to provide on-the-ground services to producers in these efforts.

Credit, Debt, and the Family Farm

Producer Payments – Price support payments from the Ministry of Agriculture to the farmers should be made directly to the farmers and not directed through the processing and slaughtering industry. Too often the payments to the farmers are retained by the processing sector and payment is not made to the farmers.

Production Credit Agency – The Ministry of Agriculture should make a loan to farmers for inputs utilized in the planting of crops. These loans will be available 60 days before planting begins. The government will have the first lien on the crops produced for the repayment of this loan. This would be a temporary guaranteed or direct credit program for borrowers who may not currently qualify for commercial loans.

Farm Credit Cooperative – The Government of Croatia should provide a one-time loan to capitalize a Farm Credit Cooperative Bank. The primary mission of this bank would be to make agricultural loans for purchase of land, buildings, equipment and agricultural inputs. These loans would either be made to individual farmers or to farmer-owned cooperatives. This loan would be repaid to the national government after 30 years.

Value-Added Tax Adjustment – Agriculture and food processing are two of the most important segments of the Croatian economy. Production agriculture and food processing are making structural changes in a climate with inadequate financing and unreliable cash flow. The national government should set up a differential value-added tax for the agriculture and food-processing sector. The VAT for this industry should be no more than 12%. The European Union has a similar VAT policy for farmers and agriculture processors.

Beginning Farmer Loan Program – The Ministry of Agriculture shall initiate a farm ownership and operating loan program targeted to beginning farmers who are qualified to enter farming but who do not have or cannot acquire the financial assets to do so. This program shall be targeted to farmers with at least five years experience and between the ages of 25 and 35. The Ministry will also provide technical expertise, bookkeeping and other training for beginning farmers through the county extension service.

Disposal of State-Owned Farmland – The national government should sell state-owned land. Fifty percent of the land should be targeted to farmers with 50 hectares or less and priority should also be given to landowners that have land adjacent to state-owned property. The state should also implement a land ownership credit program to complement the lending activities of the Production Credit Agency.

Access to Agricultural Technology and Research

Liberalization of Approval Policy of Seeds and Genetics – The Ministry of Agriculture should accelerate the approval policy of seed and genetics. It is appropriate for the Ministry to safeguard Croatian farmers and consumers by screening genetic material that enters the country. However, if Croatian farmers are to be competitive in the international market, they need to have access to the best plant and livestock genetics possible. The productivity of Croatian agriculture is hurt by the current highly restrictive regulations of the Ministry of Agriculture.

Research Priorities – A committee of farmers, processors, agriculture extension agents and Ministry of Agriculture representatives should be formed to consider the long-term research needs of Croatian agriculture. This committee should make recommendations to the Minister of

Agriculture so that public research funds are directed to the greatest needs. A survey should also be conducted of any private agriculture research with the hope that all research activities in Croatia can be coordinated to derive the greatest benefit for producers and consumers.

Rural Development and the Family Farm

The key to successful rural development is to stabilize, strengthen and build upon the agricultural base and the family farm structure of rural Croatia. Economic diversification must be a supplement to, not a substitute for, a healthy agricultural economy and a strong private farm system.

The rebuilding of the family farm system occurs when farming is profitable and agricultural opportunities are created for a new generation of beginning farmers. A positive agricultural policy can be the most immediate and effective means of enhancing rural economies, income and purchasing power.

The organization of cooperative enterprises, which retain equity, control and ownership within rural communities, is a proven self-help, homegrown, rural development mechanism that builds needed economic infrastructures for rural people. Access to credit, technical expertise and markets are essential ingredients in securing opportunities for rural and agricultural enterprises.

Transportation – We favor an integrated transportation system of waterways, railways, and roads. Maintenance of a viable, competitive transportation network within Croatia is of crucial importance to Croatia's farmers. It is particularly important that producers in the primary agriculture production region of Slavonia has access to the important tourist market on the coast of Croatia.

To ensure the free flow of farm products to the market, national transportation policy should foster and maintain a balance of competition between all modes of transportation and maintain protections for transportation users in those areas where such competition does not exist. Because of the importance of transportation to the timely movement of inputs and the movement of commodities, it is important that the government monitors access to transportation for producers and agribusiness.

Farmers and Their Organization

Realization of democratic aims and ideals requires citizen participation in the processes of government as individuals and as members of people-oriented movements and organizations.

The Slavonia-Baranja Farmers Union serves its members by providing an organizational structure in which they can participate more effectively in the processes of our society.

The far-reaching objectives of the Slavonia-Baranja Farmers Union challenge us to make the organization a strong, hard-hitting force. This requires dedicated efforts of officers, leaders, and grassroots members to strive toward the goals expressed in this policy declaration. Participation of all members of the family should be encouraged in this effort.

We urge all members to become more active in their own organization and in their local cooperatives, and we urge their active participation in state, regional, and national public life.

Active participation can best be inspired if there is attention to the study of issues and decision-making in the Farmers Union, carrying out group efforts to implement policy, and attracting more members into the organization. Members of this organization should initiate and work with other organizations at community meetings to educate people on the importance of agriculture to the local economy, the effect of trade on commodity and livestock prices, and the importance of investment in agriculture. Alliances should be built with organizations of similar views like food processors, livestock growers or associations for small and medium businesses.

Attachment D Agriculture Messenger, July '99 and September '99 issue

The Agriculture Messenger

An agriculture information newsletter

Osijek, July 1999

Issue number 2

POTATO

(*Solanum tuberosum* L.)

by Prof Mladen Jurišić

COMMERCIAL IMPORTANCE

Potato is a perennial plant. Its commercial importance is very large. It is used in human nutrition, prepared in various ways. Potato is a good fodder. In world production of crops, potato takes an important place along with wheat, corn and rice.

Potato production in the Republic of Croatia substantially lags behind the production in the developed countries. Average yield of only 9.92 t/ha classifies us at the production level of Denmark and Japan at the beginning of the century. Some producers in our country produce 30-35 t/ha but the average yield is far below the level preferred by agroecological and edaphic possibilities, e.g. the Netherlands 40-50 t/ha.

One of the prerequisites for potato production is to increase processing with adequate storage area. It is also necessary to create conditions on small family farms, i.e. enlarging surfaces planted with potato, irrigation, improvement of agrotechnical measures, adaptation of each variety to the adequate set of agrotechnical measures, application of quality and approved seed with

adequate fertilization and protection of potato. In the Republic of Croatia all varieties listed on the list of varieties issued by the Ministry of Agriculture and Forestry may be produced. Introduced and domestic varieties are previously tested within the official variety experiments monitored by the State Variety Committee.

In Croatia "white and red" potatoes are still being bought, which means the two most widespread varieties - Jaerla and Desiree. Desiree is a medium late plastic variety and a worldwide known and reliable one. Bintje is also a foreign variety known for its exceptional quality ("quality standard"), and currently cultivated somewhat less, due to the introduction of some new varieties. At the coastal area, islands, and in Istria, Jaerla is the predominant variety, followed by other early and medium early varieties: Sirtema, Saskija, Ostara, Resty, Bintje. Among the newly introduced early and medium early varieties Cleopatra, Ukama, Monalisa, Berber, Timate, Arkula and others are spreading, and among our early varieties Stanka and Dalmatinka and medium early Nada and Dobra. Once widely spread Slovenian variety, Igor, has been almost completely taken out of production because of its exceptional sensitivity to Y-virus (bacterial ring rot, manifested in blisters on tubers).

The Croatian list of varieties was enriched in 1992 with Romano and Kondor (medium early-medium late variety) and in 1993 with five new varieties (Agria, Ausonia, Sante, Concorde, and Monalisa-medium early to medium late varieties). Currently there are some thirty new varieties being tested and some new ones are expected to be added to the list.

Among the above-mentioned varieties, there are several quality varieties for food and processing (chips, pure, pommes frites and alike), and not so many starch industrial ones.

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It is of special importance to satisfy a range of agrotechnological requirements of the varieties, in order to use their genetic potential as adequately as possible

Mineral fertilization is used as a necessary supplement to the organic fertilization or as a part of full potato fertilization (if organic fertilization is missing) This fertilization is based on the addition of three basic macroelements (N, P, K) and small quantities of other nutrition elements All three elements have a great influence on the size and quality of potato yield, and favorable effects of fertilization may be achieved only in regular formulation and relation to these elements and their application, when it is most acceptable from the point of view of plant physiology

The quantity of potato mineral substance should be based on chemical analysis (EUF method) and requirements regarding the above mentioned potato nutrition For yield of 30 t/ha potato, the following quantities of available nutrition are necessary

Table 4 Necessary pure nutrition in potato fertilization

PURE NUTRITION	EARLY POTATO (KG/HA)	LATE POTATO (KG/HA)
Nitrogen (N)	100-140	140-200
Phosphor (P ₂ O ₅)	110-150	110-150
Potassium (K ₂ O)	160-260	200-350

In combined type of nutrition (organomineral), that is when the crop has been nurtured with 25 t/ha stable manure for the planned yield of 30 t/ha potato, the basic soil treatment (before deep plowing) must be fertilized with ca 60-80 kg/ha nitrogen, 60-110 kg/ha phosphor, 120-160 kg/ha potassium

Potato is rarely sidedressed, and the necessary quantities of nutrition elements must be added in autumn (main fertilization), as in the course of vegetation, plants absorb the additional nutrition quantities to the maximum From the point of view of scientific research and practice, each subsequent addition of nutrition elements do not have substantial justification The following combinations, found in stores, are recommendable NPK-7 14 21, 10 20 30, 10 30 20, 7 20 30, 8 26 26 or similar ratios

The nitrogen quantity is adjusted by adding UREA 46% in the basic treatment until complete saturation is achieved

Health condition has an important role in potato production With low quality seed material no production results can be achieved in spite of good agrotechnics In the Republic of Croatia, where potato is the third most produced crop, production yield is among the lowest in Europe (8-10 t/ha), partly because of the insufficient use of approved and declared seed material Healthy seeds are applied only on 3-5 % of the arable land Their application in the developed countries is as much as 4-5 times higher in combination with the regular application of agrotechnical measures

BROILER RAISING ON A SMALL SCALE

by John Blake

Broiler meat (a chicken weighing 1.5 to 2.0 kg) is an excellent source of proteins, and can be served in many ways (fried, baked or roasted) A small flock of 50-100 broiler chickens can easily be taken care of by a family with a minimum of labor involved Broiler feed accounts for 65-70% of the total cost of producing the broiler, which can be slaughtered in 6-7 weeks After cleaning the house another batch can be started Sanitation is of utmost importance for minimizing the spread of diseases A small broiler house with good ventilation is required The guidance of a veterinarian for disease control would be helpful Space required for the broiler is 10-12 per square meter For small flocks (10-15) electric light bulbs underneath a small canopy serve as a heat source Infra red bulbs specifically designed for chicken breeding are also available A special ration for broilers is available at feed stores A simple feed trough can quite easily be constructed Watering devices are also available on the market Wood shavings or wheat straws are used for the litter, using about 5-6 cm Litter is removed after each batch of chicken is sold The manure is especially rich in Nitrogen and is a good garden fertilizer

CONTAGIOUS SHEEP LIMPING DISEASE

by Oljeg Papac

Contagious sheep limping disease is a disease of sheep regardless of their sex, breed or age, located between hoofs or on soft parts of hoofs. This disease is rather spread in Croatia and can infect goats occasionally. The agents of disease are *Bacteroides Nodosus* and *Fusobacterium Necrophorum* that die relatively fast, in dry environment in seven and in humid in 14 days.

The sources of infection are ill sheep, carriers of infection, sheep that do not show signs of illness can also carry the infection on their hoofs, contaminated pastures, bedding and outlets where contaminated herds live.

New herds can get infected through new, infected animals brought to the herd or by coming to the infected areas, paths, folds, etc. Contagious sheep limping disease favors humid weather and damp terrain, folds, etc.

The disease agent enters the skin through hoofs and from there penetrates the soft parts. The process is enhanced by moisture, keeping of sheep on wet bedding as well as injuries on the skin between hoofs.

Incubation lasts for 10-15 days.

The disease usually does not spread outside the hoofs. The symptoms at the location of infection are redness, swelling and dead tissue. The disease advances quickly starting from soft parts (heels), towards the top of the hoof. As a consequence, corium dies out, hoof festers and bony core separates from foot and starts decaying with a very unpleasant smell. The process of inflammation usually spreads to surrounding tissue, tendons and joints that can result in complete separation of the hoof from the feet as well as in phalanxes falling off.

Sheep react by limping that is extremely visible on a hard surface. Sheep can limp on one or more legs. When front legs are infected, the animal is walking on its knees and lying most of the time and if all four legs are infected, the animal moves with extreme difficulty.

The losses encountered are due to decreased production of meat, milk and wool as well as by costs of treatment.

The disease is treated through surgery and chemotherapy. The rotten part of the hoof has to be removed through surgery, making sure that healthy tissue is not harmed and there is no bleeding. During the lopping of a hoof, healthy bony core should be corrected. After the rotten part of the hoof is removed, a disinfectant is applied locally. Good results can be achieved by dipping the hoofs in 10% formalin for 15-20 seconds or by covering hoofs with 10% chlore-micetin tincture, cetavlon or teramicin grease. Therapy is repeated one or two times and with deeper injuries up to three times. The sheep that are being treated must be held separately from the rest in a dry place. The cut parts of hoofs should be burned and all lopping instruments held in 10% formalin. The sheep is considered healthy when its hoofs have healed entirely.

Preventing the disease and stopping an epidemic is closely connected with the treatment of sick sheep. Sheep that undergo a treatment should be held on uninfected terrain in the driest conditions possible. Sheep which are suspected to be infected should first be taken through a water pool to wash hoofs, after that through another pool with 5% CuSO_4 (blue copper) and then kept on an uninfected pasture or fold.

The contaminated terrain cleans itself in seven days of dry weather or 14 days of humid weather. It is recommended that a system of pastures be established, considering that sheep can return to the same pasture after

14 days. Putting new sheep in quarantine will prevent new infection of a herd. It is also possible to inoculate the healthy herd with a

vaccine prepared from inactive agent of the disease

Purchasing Power of Associations

by Tihomir Gorša

In the first edition of 'PG,' the US volunteer consultant Martin Clark wrote an article about associations in Iowa that transport livestock to markets outside the area of production in order to realize higher profits in markets offering significantly higher prices. While Mr Clark provided an example of how associations help private farmers from the marketing side of agricultural production, it is important to understand the benefit that associations afford farmers on the purchasing side of their businesses.

For example, at a meeting which FLAG-Petrinja hosted in early June, seven farmer association chairs representing seven associations that FLAG-Petrinja helped to

form and subsequently sign as clients met with the owner of a local farm supply store about planting inputs for next season. The associations agreed to collect data on their requirements for seeds, artificial fertilizers and pesticides for the next season, and prepare a large request for quotation for the entrepreneur in order to receive a reduced price at approximately 30% discount. The price includes the delivery to the farmers in their respective villages – so far, farmers were forced to provide their own transportation. Once the bid is prepared, FLAG-Petrinja will assist the associations present it to other suppliers in order to receive competitive prices. The purchasing power made possible by farmers organizing themselves in associations that they control provides a concrete example of the benefits of farmer-controlled associations.



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The Agriculture Messenger

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Dear readers,

We would like to inform you that from this issue on, you will be able to read about the experience of our friend Mr Mirko Macokatic, in addition to our standard articles. Mr Mirko Macokatic (Croatian Cooperative Alliance – Osijek Baranja county) was part of a group that went on a three-week training trip in Missouri, as a part of FLAG training program, sponsored by USAID. The goal for the group was to familiarize themselves with the work of cooperatives in the US and gain knowledge that will be helpful in the future work with cooperatives in Croatia. We hope that his experiences will be helpful to you as well.

Greetings,

Anita Falamic

RECORD KEEPING

by Dr Toney Reynolds

Management requires many tools and skills. One of the most valuable management tools in any business is record keeping. Farming enterprises are no exception.

Record keeping does not have to be really elaborate or complicated. A simplified method for the business involved is the best policy.

Keep in mind, record keeping is of no value unless it is used for a purpose. Records should provide direction for the business so that the business can continue to grow and become more profitable. If a business is not profitable, then a change would probably be in order.

Records are most important when applying for credit to lending institutions. They are also important when considering the purchase of new equipment. In the United States, farmers that do not have good records go bankrupt possibly two years before they are aware of it.

In pig production, records should reveal sows that are most profitable, such as, number of pigs weaned per litter, number of litters per year, cost of gain on the offspring. In order to make good selection for replacement gilts, good record keeping will show you the cost of your production, the return on your investment and projections for the future. In any enterprise or undertaking, there should be a primary goal and an alternate plan if the primary does not prove profitable.

Same criteria should be applied to dairy cows, sheep and goats. In other words, a farmer with a flock of sheep should be able to determine ewe lambs from a good producing ewe. Things to consider in making this choice would be weaning weight, gainability, conception rate of the mother, ease of lambing and resistance to diseases, etc.

Of course, in order to keep good records of value, you must be able to identify the parent by number or other means. **DO NOT TRY TO COMMIT THIS VALUABLE INFORMATION TO MEMORY.** You must have it in writing. Lending institutions and banks are impressed with good records. I

In this issue

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would like to emphasize once again the value of putting this information to good use

I find in my experiences that farmers, who keeps accurate records prosper more than those who do not keep any records at all. The main reason is that they are much more aware of the cost factor and utilize time and material to the best advantage possible

FLAG ACTIVITIES IN THE KNIN AREA

by FLAG Knin

One of the most recent activities of the FLAG Knin office has been developing a joint venture between the Lutheran World Federation, based in Finland, and FLAG Knin which involves sheep farmers in the Otocac-Korenica-Udbina area. In this project, LWF finances the purchase and transportation of pregnant ewes of the Pramenka breed from Rumania and places them with disadvantaged families in the area. Over 1000 sheep will be placed with 200 families this month, resulting in five sheep for each family. The male lambs will be sold for food in the spring, creating a source of income for the farmer, while the female sheep will be kept to breed in an effort to increase the number of sheep in Croatia as compared to pre-war levels.

FLAG's role is to assist in organizing a sheep-breeders association, based in Licko-Senjsko County. Through this association, FLAG will provide training on proper feeding and care for the sheep, including the lamb crop that will arrive in January or February of next year. FLAG will also assist by helping provide the necessary grain feed supplements to the farmers, as well as by organizing the farmers into an operation that will, if all goes according to plan, sell sheep milk to a major cheese producer in Otocac. The benefits FLAG brings to the association are healthier, bigger lambs that will make more money for the farmer when they are sold, as well as a potential source of income from milk sales.

Such examples show the usefulness of local farmer organizing to farmer-led associations. Without some organizations, the farmers would not have access to grain feed for their lambs, nor would they be able to sell their milk on a sufficient scale to make a profit. This would result in improved information exchange, marketing efforts and coordinated meat and milk sales.

FLAG will assist the association by providing seminars on such items as proper nutrition for sheep, correct lambing procedures, disease control and care for lambs. FLAG will also organize through the association cost-effective ways of procuring veterinary services. These vet services will be important in keeping lamb mortality rates low and reducing diseases and infections. Pete McNeill, a professional and experienced sheep breeder from Kentucky, USA, will conduct the first set of seminars on the importance of record keeping towards proper flock management.

It is obvious that associations will be a key element in the future of Croatian agriculture. This project will be duplicated in different municipalities and across multiple types of agriculture, resulting in increased information exchange, economies of scale in input purchases and ability to encourage political leaders to focus on farmer needs. FLAG Knin is excited about the potential of association building. Interested producers can call Damir Buntic at our office at 022/661-158.

FLAG ACTIVITIES IN THE PETRINJA AREA

by FLAG Petrinja

On September 9, 1999 FLAG-Petrinja organized a large agricultural meeting/trade fair on the premises of the Gavrilovic plant in Petrinja. Mr Gene Hodgkins - visiting agricultural volunteer and Mr Tihomir Gorša - FLAG-Petrinja's Agricultural Advocate initiated the meeting. Agricultural producers, marketers, representatives of firms in agribusiness, NGOs, and FLAG personnel made contacts to talk business with each other. Four visiting FLAG agricultural expert volunteers from the US: Mr Peter McNeill (sheep), Mr William Lord (beekeeping), Mr Tony Reynolds (veterinarian), and Mr Gene Hodgkins (farmer association formation) conducted a Q&A session with the farmers. Participants also got acquainted with the concept of the FLAG/Croatia program and results to date.

Mr Alan Chelko, FLAG Regional Coordinator for Former UN Sector North (FLAG-Petrinja), opened the meeting with a presentation on the various FLAG agricultural initiatives. Mr Gavrilovic, President and owner of Gavrilovic d.o.o., followed with a discussion of his close co-operation with FLAG and further explained what Gavrilovic as a

company is doing to improve agricultural production in the region. Mr Gavrilovic stressed the need for farmers to focus on quality and praised FLAG for its efforts for training farmers in the production of quality livestock. The final speech was delivered by Mr Mark Grubb, FLAG-Croatia Country Director. Mr Grubb discussed agricultural policy reform points that FLAG has put together with the guidance of visiting professional agricultural lobbyists from the US. He stressed on the fact that the farmers themselves should be involved in creating a document to be presented to the Croatian Government. He emphasized the need for farmers to organize themselves in functioning and effective organizations, to speak for themselves in the public forum, and to work closely with FLAG on all agricultural issues which effect their ability to produce and market their respective products.

The meeting was a pronounced success. FLAG received favorable feedback from all participants. Key marketing linkages were made during the event. Participants had the opportunity to meet their counterparts in the Croatian agricultural community and the visiting experts, and to get acquainted with the FLAG program and staff.

THE CO-OPERATIVE MOVEMENT IN THE UNITED STATES

by Mirko Macokatic

Co-operatives are highly developed in the United States. Each American is a member of at least one co-operative (agricultural, credit union, buying-and-selling, electrical co-operative, etc.)

The co-operative is primarily the most suitable form of organization of village economy (the term village being conditional) as well as of some other economy sectors. The co-operative outgrows the narrow interests of the individual, concentrating on the interest of the larger, broad community. It is especially suitable for activities targeting larger number of people. Its internal organization and control mechanisms do not allow the negative tendencies that often affect corporations.

The etiology of co-operative movements is the same worldwide. Americans are very proud of their long history of co-operative movement that goes back to the beginning of the century. At that time, the

economy and agriculture survived the great depression and farmers, regardless of the size of their farms realized the importance of associations that allowed them to jointly supply themselves with inputs, expertise and the ability to sell their products and develop.

In the 1900's the territory of the state of Missouri was electrified (St Louis). In the 1920's railway tracks were intensely laid and new roads constructed in the central part of the US. New markets opened. It is to be noted that the establishment of co-operatives occurred in the years of prosperity. Could there be a better climate than that for establishing and confirming the positive attitude towards the new type of association?

The functioning of US co-operatives is characterized by the continuity of the process. They have never seized operation, nor suffered human or material losses as it happened in Croatia, during two world wars and the 1991 war. It is important to mention that American co-operatives were never misused and forced to act against their own membership as it happened here after World War II, during the process of compulsory collectivization.

US co-operatives have 90 years of steady development history.

Various types of co-operatives exist in all areas of the economy. Although our focus is on agricultural co-operatives, most of the elements regarding the foundation, work practices, internal relationships, management, property and responsibility are applicable to other types of co-operatives as well.

Agricultural co-operatives can be farming, cattle breeding, dairy, swine or other types. Their characteristics are complexity and specialization. The main services they provide are supplying members with inputs, finding markets for their products and selling the products. They sell products and charge for that services. Co-operative can provide storage for commodities as well, although American farms are usually equipped with their own storage, drying, calibrating and packaging facilities. Furthermore, the co-operatives can provide repair services and maintenance of mechanization and equipment, as well as other agricultural services. Co-operatives give no loans. Farmers that need a loan, can get it from a credit union or a bank. Co-operatives should work in close cooperation with consulting agencies.

One of the characteristics of American economy is specialization, which leads to high

effectiveness American farmers, striving to improve their living standard, aim at increasing their production per land and per cattle. The co-operatives do not own land nor have their own agricultural production.

Regarding the essence of work done in the US and Croatian co-operatives, we can conclude that they are fairly similar.

The size of co-operatives is not regulated but basically they are quite big. Their present size is the consequence of a natural trend in uniting people in traditional, economic, infrastructural and culture groups. Some of the co-operatives unite thousands and even tens of thousands members. From geographical point of view, there is practically no area without a co-operative.

Co-operatives are managed by their members. There is a high degree of trust among members, the Assembly and lower management bodies, primarily the Board of Directors and the Manager. The Assembly consists of all members, but the size of membership is so big that it is practically impossible to gather all members or even a majority. There are two solutions to this problem. The bylaws of the co-operative define the quorum, requiring 1/10 of the total number of members to be present at the Assembly or the membership of the Assembly is determined on the basis of the principle of representation.

The Assembly, similar to the practice in our country, makes important decisions and determines strategies for the co-operative's business development. The Assembly meets at least once a year.

The Board of Directors is a subordinated body that meets on regular basis. The overall organization of co-operatives and the techniques for achieving the goals of members in accordance with international co-operative principles, make the size of the Board of Directors an advantage, with its flexibility and better efficient.

The Manager is a person of great confidence among the members. The authority of the Manager is usually limited, regarding legal practices such as instance and handling of co-operative property. The co-operative Manager and employees are paid salary for their work.

One of the objections made to Croatian co-operative practices is the possibility of both the Manager and employees to be members of the co-operative. In the US, there is no provision prohibiting the Manager and

employees to be members of the co-operative, nevertheless the situation does not occur, for two main reasons.

First, the Manager and employees of the co-operative do not own a farm. They do not have the necessary capital to buy land and if they did, they would be so busy taking care of it that they would not be able to work for the co-operative at the same time.

Second, the Manager and employees are not motivated to become members of the co-operative. Profit is distributed only among members who do business with the co-operative, while the Manager and employees do not do any business with the co-operative and cannot participate in the distribution of profit.

Farmers can be and usually are members of several co-operatives of different type: general, dairy, etc. They can be members of more co-operatives of the same type as well, although such cases are not popular. The reason for this is that co-operatives are managed by their members.

There is no competition among co-operatives in the same area of operation, again because members do not have the need for new co-operatives and even if that is the case, it would be difficult to compete with existing co-operatives that already have significant capital, infrastructure and staff.

Why do US farmers join co-operatives?

- 1 For the supply of equipment and inputs for production, where a co-operative makes a better deal than an individual can,
- 2 For better marketing of products,
- 3 For expert assistance,
- 4 For better development programs.

Farmers can work on these performs individually. There are no regulations or other provisions forcing them to enter co-operatives. Still, they are driven into co-operatives by the logic of economy. An important reason for becoming a member is the profit and participation in its sharing.

Farmers, in protection their own interests, have worked out precise mechanisms of monitoring contributions to profit and its distribution.

The requirement for participating in the distribution of profit is to do business with the co-operative. The cooperation and its amount are being closely monitored to avoid overflow of profit from profitable to non-profitable activities. This requires accurate and record

keeping Each member's share in the profit is proportional to the volume of cooperation

The members are monitoring the operational costs of the co-operative There is no luxury in the co-operative's offices, some often look worn-out because members prefer to spend the cash on their farms

However, part of the profit is retained by the co-operative and accumulated in a fund In the case of liquidation, or a membership cancellation, the member is refunded, although not immediately the entire amount (the period can extend up to 10 years) This and other regulations provide protection to the property of the co-operative and its members

In order to become a member, the individual usually has to meet the requirement of doing business with the co-operative of \$500-\$1000 in value If the volume of cooperation is permanently bellow the minimum, or cooperation ceases, the membership is cancelled and the farmer is entitled to collect his share in installments In the case of member's death, the inheritors are entitled to the share

Members can have more than one share in a co-operative, however, that does not entitle them more than one vote With no exception, the voting principle in co-operatives and other associations of co-operative type is one member, one vote When a member makes improvements to his farm, participates in the profit according to the contribution, and that contribution is measurable, the farmer's rights are not object to subjective evaluation If all business operations can be transparently monitored, recorded and verified, then really no member needs more than one vote

THE FOUNDING OF THE CO-OPERATIVE

A co-operative is a legal person and the bylaws define the relationships among members, as well as the activities, methods and management Members pay their fees, the amounts of which as well as that of the capital are not regulated

Members acquire initial capital and present themselves in a convincing manner to financial institutions and business partners The legal fee for chartering a company - compared to requirement in Croatia - is symbolic, from \$5 to \$250

The cooperative chartering is performed by the Office of the Secretary of the Federal State The procedure is very simple and the

purpose is more to register the co-operative as a taxpayer than informing the businesses about the new subject Finally, even in our country the information about the subject, its activity, property and reputation are learned from sources other than newspapers and the National Gazette, which are quite expensive, by the way

The organization of co-operatives and farmers' goal to achieve higher results with existing specialization and lower investments, lead to directing their efforts towards increasing the production per land and per cattle with lowest costs

The farms and co-operatives remained at the level of producing raw materials that had consequences on the prices of basic agricultural products, semiproducts and final food products as I will describe them in the chapter dealing with the position of farmers in Missouri All that places farmers in a difficult position, decreased the number of farms and farmers

A very interesting information is that although the state of Missouri is a significant producer of swine and beef cattle, a single important industry of swine or beef meat is not to be found there

In order to eliminate the above described negative trends, the government decided to assist, not with durable subsidy program, but with a program supporting the establishment of a new generation of co-operatives, the processing type of co-operatives (ethanol, pig slaughter houses), offering very favorable conditions

In the Taxation System Chapter, I will give an example of funding of such new generation of co-operative There, I will also describe the taxation system and subsidies in agriculture I would only like to point out that co-operatives are considered non-profit organizations in the US That does not mean that the co-operative is not trying to make profit, it definitely is, but not for the co-operative itself, not for the accumulation of co-operative assets but for the accumulation of wealth of its members For this reason, the profit is not taxed but shared among members

THE ASSOCIATIONS OF CO-OPERATIVES

In the US co-operatives join associations, but their system is different than the European one Since the foundation of any agricultural system is a farmer, its origin is again a farmer, the organizational forms are only mechanisms for the well being of farmers

A strong form of farmers' organization are associations of farmers which are independent, not belonging to any political party, non-governmental, united and very powerful. Not a trace of influence of any political party can be found in farmers' associations.

Farmers associations are extremely strong, possessing huge property, real estate and expertise, so that the large part of activities performed in Europe by the Association of co-operatives is in the US done in the farmers' association.

The Association is a place where the strategy for lobbying is developed, and that is not an ad hoc activity but a permanent process, which requires constant informative exchange among farmers and interaction between farmers and the public sector.

Those activities include creation of political platforms and gaining the support of politicians for their goals, strong support to such

politicians especially during the election campaigns, providing politicians with expertise, especially in agriculture as well as monitoring of activities and behavior of both "their" and opposing politicians (primarily voting).

When business is concerned, the co-operatives join so-called Co-operative corporations, similar to our business associations. The motif for uniting is business and the logic is clear to unite, act together, be stronger. As there is no farmer who is not a member of some co-operative, there is no co-operative that is not a member of a business association. Such association makes profit as well, with a purpose to distribute it among the members following the principle of proportion between the contribution in making profit and the share in earned profit.

So many similarities between our and US system, yet so many differences.



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ATTACHMENT E SURVEY OF THE MONTENEGRO TOURISM INDUSTRY

**FLAG -- Montenegro
September 27, 1999**

EXECUTIVE SUMMARY

This USAID funded study assesses the Tourism Industry in Montenegro and makes specific recommendations for developing its potential. Although major impediments currently exist, Montenegro has the ability to substantially increase its revenues from tourism. Potential travelers find it difficult to obtain information, access by air or vehicle transfer from Dubrovnik is essentially impossible, and once the traveler arrives he is forced to use cash. These conditions force Montenegro to rely on foreign tour operators who hold all the market power. Since they have no investments in Montenegro they will divert their customers to other locations when convenient. Montenegro is drifting towards an image of “sun, sand and sea” with little effort to differentiate itself from mass tourism destinations such as coastal resorts in Spain or Turkey.

Montenegro should develop its tourism potential as a four season, multi-experience, high quality, “European” resort destination for middle to upper income world travelers. To achieve this vision tourism infrastructure should be upgraded to the desired market and the wealth of tourism products marketed to individual segments. While pursuing this strategy Montenegro should focus in the near term on the Eastern Europe market, West European Tour operators and KFOR/ NGO personnel serving in the Balkans.

Access needs to be improved with international flights into Tivat and Podgorica airports. Montenegrin Airlines needs to join an airline computer reservation system and to link with an international partner. Convenient land transfers from the Dubrovnik airport need to be established. The banking system needs to provide for credit card acceptance and use of ATM machines and travelers’ checks.

The state owned hotel firms are essentially bankrupt. Rapid privatization will provide both entrepreneurial managers and investment capital. Immediate action to award management contracts for selected hotels to international hotel firms would provide professional management and necessary capital for refurbishment. Hotels waiting to be privatized need to be linked to a computer reservation system. Performance of individual hotels and managers should be benchmarked against attainable standards and managers held accountable.

Montenegro was marketed as a subset of Yugoslavia without significant name recognition of its own. The State should retain an international public relations firm to promote the image of Montenegro as a desirable location for international travelers that does not involve the ethnic strife associated with the Balkans. Montenegro is more than a summer beach resort. The Tourism Board needs to segment the market and direct specific campaigns at each target group.

Success in unlocking the tourism potential requires more than just the efforts of the Ministry of Tourism. Ministries and local governments need to create the environment that supports local entrepreneurs who will eventually be the engine to achieve Montenegro’s success.

OVERVIEW

Study Purpose

The Government of Montenegro, through the support of USAID, secured the assistance of FLAG (Firm Level Assistance Group) to assess the tourism industry and to make specific recommendations for developing its potential.

The guidelines for the project were to

- Assess current situation of the Tourism Industry
- Assist in the formation of a strategic vision
- Identify specific actions to regain market share from the European and North American Market
- Identify markets for the transition period to assure high utilization
- Propose strategies to replace low rate mass tourism with quality leisure travel

FLAG performed the study using a local tourism consultant familiar with existing conditions and an international tourism consultant with extensive experience in Eastern Europe. The three-week in-country phase consisted of visits to major coastal and mountain resorts. The Ministry of Tourism supported the project by assigning a full time project manager. Meetings with key government agencies that influence tourism were held. The FLAG Team inspected over 32 hotels and interviewed more than 100 people.

FLAG acknowledges the special efforts of Ljiljana Vujinovic, Senior Adviser at the Ministry of Tourism, for her advice, and her efforts in arranging the appointments with government officials and industry leaders. Zeljko Uljarevic, local industry consultant, provided important insights concerning existing conditions. Without exception, government officials and tourism executives graciously offered their valuable time to give insights into the state of the industry. Observations and the information provided by government and industry leaders provide the basis for this assessment.

The Government of Montenegro recognizes that major policy changes are needed to unlock the economic potential that tourism offers. To provide focus as the Republic develops its potential through specific actions outlined here, FLAG recommends that Montenegro adopt a strategic vision.

The proposed Vision Statement is

Develop the economic tourism potential of Montenegro as a four season, multi-experience, high quality, “European” resort destination for middle to upper income world travelers.

Realization of this vision will necessitate establishment of a State Tourism Model with specific state economic impact goals for the tourism industry to benchmark against other successful countries that have adopted a similar model (Switzerland, Ireland, Malta, Portugal, and Slovenia).

To Meet This Vision, Specific Objectives Include

- Redirect the market to the middle & upper market segments
- Upgrade the tourism infrastructure to future target market levels
- Link the various tourism products to specific targeted markets
- Unlock the full potential of Montenegro’s tourism assets
- Create a four-season tourism industry
- Maximize the economic potential of each location

Recommendation Summary

To achieve these objectives the following actions must be pursued

- Open the borders and airports through diplomatic channels
- Pursue joint use of Dubrovnik Airport
- Provide a banking system that supports the tourism industry
- Pursue management contracts with global hotel operators
- Accelerate privatization in order to obtain investments to upgrade hotels
- Secure investors who are backed by “global hotel brand” operators
- Contract with an international public relations firm to develop and promote an image for Montenegro
- Develop a professional Internet site that provides information and allows booking for hotels and other tourism services
- Join Montenegro Airlines to an existing alliance of international carriers
- Upgrade hotel facilities to their original ratings and the highest market potential
- Link hotels to a Global Distribution System (GDS) to facilitate reservations
- Shift the responsibility for “Bed Nights” generation from the State to Hotels
- Retrain Hotel managers in Western Finance & Marketing Management
- Replace low income producing properties in “prime” coastal locations
- Control land speculation and development by assessing land values based on “highest & best use of land” and differential tax structures
- Create a special tax and licensing structure for all low revenue producing resort properties such as “company” hotels and non-residential “vacation homes”
- Stop the building of “Grey Market” vacation homes (Budva/ Sutomore)
- Consolidate all coastal community development plans into a Master plan and consider new projects only on the basis of demand or unique new offerings

Many of these actions will require time to implement Therefore Montenegro should pursue near term marketing strategies These include

- Generate cash flow in the near-term by focusing on the Eastern European and Russian markets
- Secure contracts with West European “InclusiveTour Operators” for the 2000 summer season
- Secure a “preferred “ position as a Rest & Recreation and family re-union site for KFOR and OSCE personnel stationed in the Balkans
- Expand Marketing & Reservation Distribution Channels

III CURRENT ASSESSMENT

Viewed from the traveler’s perspective, a visit to Montenegro entails several major impediments Even assuming that the traveler has heard of Montenegro and decided to visit there, he will find it extremely difficult to obtain information A casual search of the Internet does not reveal any site devoted to tourism in Montenegro Most travel agents are not informed about the tourism opportunities there Coming as an individual traveler to Montenegro is essentially impossible Even if the potential visitor ignores travel advisories issued by various governments, and flies into Dubrovnik, there is neither organized transportation nor an opportunity to rent a car that can be taken into Montenegro The visitor will find it difficult to make a hotel reservation prior to his arrival Once in the country, he will not be able to access ATM machines, cash his travelers checks,

or pay with credit cards. He will instead need to bring cash, and will be forced to change money on the street to obtain local currency.

These significant hurdles force Montenegro to rely on the domestic market and on mass tour operators. The mass tour organizations hold the market power, and without any credible alternatives Montenegro's negotiating position with them is weak. Tour operators have little financial incentive to maintain long-term relationships and will change their programs at the slightest sign of trouble.

A specific assessment of current key sectors of the tourism industry follows.

The Hotel / Lodging Industry

The Hotel Industry is comprised of 93 hotels (excluding tourist settlements) with 15,000 rooms. Survey findings concluded that Montenegro presently has only 2,000–3,000 beds and 1,000 to 1,500 hotel rooms in the current inventory at a quality level that can be marketed to Western European / American travelers. (See Appendix B for a listing of hotels that are only marginally qualified for international guests.)

The capacity of the industry is approximately 150,000 beds. About 50% of the bed capacity are in private homes (not including the Grey market) and 15% in factory-owned "company" hotels. These facilities were not included in the inspection and review process but it can be inferred that tourists staying at these facilities produce minimal revenues and taxes but generate significant expenses to the communities.

Except for domestic use, hotel beds are mainly marketed and sold by contracts to major European wholesale / charter operators at daily rates per person / half board of about DM 25-45. Tourism receipts totaled approximately \$250 Million Dollars before the de-stabilization of the Balkan region in the early 1990's. The combined tourism / catering sector of the economy dropped to \$86 Million Dollars in 1998. This total represents less than 10% of GDP.

Montenegro has an excellent opportunity to increase tourism income by capitalizing on its quality tourist offering. This will necessitate a gradual reverse in its market position from the "Low Budget" market to a "Quality European Resort" market. The definition of Montenegro as a "Mediterranean Resort Destination (Sun, Sand, and Sea)" should be reviewed in view of the excellent recreational opportunities also offered in Montenegro's mountain regions.

The hotel industry, organized primarily into 4 large and 15 smaller companies, is state owned and practically bankrupt. Due to a lack of business and to high fixed costs, most hotel companies cannot meet their current expenses. Account balances are negative and long-term debt is not repaid. One notable exception was the Ski Center in Zabljak. The management team there not only generated an operating profit through aggressive sales and good customer service, but also made investments in the resort infrastructure out of operating cash during the crisis years.

Most hotel companies operate with twice the number of employees they need for current business levels. Few hotels operate year round, many are opened only for the summer period. Due to a focus on social needs, positive cash flow (if any) is used for social purposes and not for upgrading of facilities. No capital investments have been made for about 15 years to upgrade and maintain facilities. As a consequence, none of the hotels has sustained its original rating in its respective category. In addition to the need for complete refurbishing, most of the hotels require high capital expenditures for replacement of plumbing and heating systems, improvements of communication, upgrading of kitchens and restaurants, and computerization.

Market Accessibility

Montenegro is primarily an air destination that has relied on Čilipi Airport in Dubrovnik and the domestic Tivat airport. Tivat currently services primarily domestic flights, but with the lifting of sanctions the recently formed Montenegro Airlines plans to begin servicing a number of European capitals. Croatia Airlines has numerous scheduled flights to Dubrovnik but most originate in Zagreb. Flying into either Tivat or Dubrovnik from Western Europe is expensive in both time and money. There is no established land transportation between the Dubrovnik airport and Montenegro. Rental cars hired in Dubrovnik cannot be taken into Montenegro. Given the trend to shorter, more frequent vacations, a destination requiring an entire day of travel to reach will have difficulty competing for travelers.

The inability of travelers to use scheduled flights and the existence of border access problems with Croatia has severely restricted travelers access to Montenegro.

Visitors can also use the car ferry from Bari in southeastern Italy to the local port of Bar.

Tourism Marketing During the Crisis Period

Montenegro attempted to open the East European market, which has a significantly lower tourist spending average than that exhibited by West European, Asian or North American travelers. Because of travel restrictions, Montenegrin tourism professionals had difficulty in maintaining active contacts with European travel partners. Travel advisories issued by various governments discouraged travel partners from sending their clients to Montenegro. This is tragic, as Montenegro remained a benevolent nation with no ethnic turmoil while civil strife raged in neighboring countries.

Management Expertise for a Market Economy

Hotel executives are not yet trained in applying western concepts of sales and reservation management nor do they have the available tools and linkages. These processes are important to upgrade the level of tourism and to increase the number of visitors. Modern management processes of planning, organizing, evaluating and controlling are not applied. Business units are not organized into profit centers nor are they managed according to the standard uniform system of accounts for hotels. The concept of using management accounting to support decision-making does not exist. There appears to be no timely comparison between forecast and actual results (i.e. no variance analysis). This situation precludes any meaningful adjustment during the year and deters management accountability. It will delay efforts to privatize key current or future high-income-potential properties through international tenders.

Destination Potential

Montenegro lies within a 1-2.5 hour direct air flight from any major West European Airport. The country offers all conceivable tourist and cultural attractions within its 3,000 square miles (13,700 sq km) of coastal and mountain regions. Untouched nature, high mountain plateaus, deep canyons, clear rivers, mineral-rich sandy beaches, a strikingly scenic fjord, and lakes and streams provide unrivaled scenic beauty. Ancient cities, rare art, and historical treasures -- combined with culture and traditions -- provide appeal to the sophisticated traveler. Good food and wine, friendly people, and favorable climatic conditions round out the Montenegrin tourist experience.

Truly, Montenegro has something to offer to every segment of the tourism market. Health tourism offers a climate superior to the central European competition. Adventure travelers and sportsmen can both pursue their activities here. Opportunities exist in the meeting, congress, and convention market, in the sports training market, and in the conventional business traveler market. Festivals with a variety of themes are held in several regions throughout the year. Quality skiing exists with the potential for significant development.

See Appendix A for a listing of attractions at particular Montenegrin tourist sites.

Economic Potential

Montenegro seeks integration in the European Community. The cornerstone of development of the tourism industry is the privatization of hotel companies. This process will attract needed capital for renovations and facilitate opening new markets. Properly focused, tourism will help promote international understanding and export. Visitors should come as tourists and leave as potential investors.

The Tourism/ Catering Industry today constitutes approximately 9% of the Gross National Product or about \$86 Million. Before the sanctions, annual turnover in the tourism industry alone averaged \$250- \$300 million. It is further worth noting that Slovenia generates about one billion dollars in tourism receipts with about the same number of beds. Montenegro, with its quality tourist offerings, has a substantial potential for growth if lodging facilities are upgraded and the market potential of each tourist center is maximized with quality (not quantity) tourism.

The price level of the Montenegro tourist and lodging market is mainly determined by contracts with major tour operators.

Unfortunately, data collected does not measure visitor spending by market and tourism segment. In addition, the total economic impact of tourism to employment, investment and taxes has not been calculated.

Previously, Montenegro was marketed as a sub-set of Yugoslavia without significant name recognition of its own. After nine years of isolation from visitors from the most developed economies, Montenegro is in a unique position to make a new start. Re-trained, profit-driven local managers, with support from strategic investment partners, can reposition Montenegro in the middle to upper class tourism markets.

This assessment is followed by specific recommendation for actions that can be taken by the Montenegrin government and the various ministries and organizations that serve the tourism industry.

ACTIONS REQUIRED

General Government Policy

- Continue diplomatic effort to open the border between Croatia and Montenegro and facilitate the use of the Dubrovnik Airport for Montenegro-bound visitor arrivals and departures.
- Seek investment for the rapid development of Tivat and Podgorica airports for international visitor arrivals to at least the standards of Dubrovnik and Zagreb airports in accordance to the master plan.

- Initiate diplomatic efforts to obtain one-year business visas to permit Montenegrin tourism marketing personnel and hotel executives to work in Europe, United States, and Asia
- Seek NATO cooperation to remove airspace restrictions for Montenegro airlines
- Re-activate the banking system to allow for timely and cost effective processing of major credit cards and travelers checks Businesses should be paid within 7 days and commission rates should not exceed 3.5 % for credit cards and 2% for Visa & MasterCard
- Renegotiate with international insurance carriers to facilitate the use of the “green insurance card” for motorists and to make affordable insurance available to car rental companies
- Stop and “reverse ” the building of “illegal” vacation homes and control the “Grey Zone” with registration levies and special taxes (Budva/ Sutomore)
Clean up the JAZ beachfront
- Move forward with strict zoning regulations for the coastal areas and the national parks
Establish traffic-free zones in each tourist and city center
- Restrict new tourism developments to quality, high-profile projects such as upscale resort condominiums and villas, golf clubs, and mountain resorts
- Implement special zoning regulation and taxes for non-resident tourist homes

IV Ministry of Tourism

- Engage a leading marketing company to advertise and promote the image of Montenegro as a desirable location for international travelers Establish a professional Internet site
Leverage the current name recognition and focus a public relations campaign on the fact that Montenegro remained an “Oasis of Tranquility” without ethnic tensions during the past eight years of ethnic strife in the Balkans
- Establish National Tourism Sales Offices in key feeder markets in co-operation with Montenegro Airlines to leverage the marketing impact In the interim, tourism specialists could be placed in Montenegro Trade Missions abroad
- Gain membership in the World Tourism Organization (WTO)
- Establish Montenegro Tourism Centers at the Tivat and Podgorica airports and a Montenegro “Welcome Desk “ at Cijepi airport, on the Croatia – Montenegro Border, and at the Harbor Terminal in Bar
- Partner with the Ministry of Culture and the Ministry of Education to bring international congresses to Montenegro
- Secure an agreement with a cruise company to start and finish Mediterranean Cruises in Kotor instead of making Kotor only a port of call on a cruise schedule
- Organize the Ministry of Tourism into 3 principal Departments -- policy and planning department, department for research & information, and department of tourism promotion and public relations.

The planning department should identify those markets that would most benefit each tourist center based on the specific appeal of a tourism offer to targeted market segments Cost / benefit ratios for each tourist community by type of visitor and by season should be developed to assist in future planning

V Privatization Issues

Montenegro has embarked on a clear path toward privatization Privatization provides a means of moving from a command to a market economy It also provides the key to acquiring both entrepreneurial managers and investment capital

The state-owned hotel firms are essentially bankrupt. They lack viable management accounting systems and are not tied into any Global Distribution Systems. No brand identity exists. Managers rely on the State to perform the marketing functions. Hotel companies typically control multiple properties in particular resort communities, but there is no competition among these hotels. In fact, individual hotels within a hotel company do not function as profit centers. Those few hotels with motivated managers lack access to the capital that is needed to upgrade their facilities. The hotels are caught in a downward spiral. As facilities deteriorate, rates decrease, which in turn reduces revenue available for needed improvements.

Each of the hotel companies has been valued by The Agency for Economic Restructuring and Foreign Investment. These valuations were reported to be based on a type of net present value analysis but in reality appear to be based on replacement value. They are unrealistically high. The real value of an existing hotel is not the cost of the plant, property, and equipment (PPE), but rather the potential -- based on a stream of future cash flows -- once the property is upgraded and effectively managed. In contrast with outdated industrial facilities, resorts have inherent potential based on their locations.

Four hotel groups are currently identified for international tenders: Institute Igalo, HTP Budvanska Riviera, HTP Ulcinjaska Riviera, and HTP Boka. It is unlikely that these companies as currently configured can be sold to owners who will invest the necessary capital to return them to profitability. FLAG recommends that Montenegro retain the services of a financial advisor experienced in hospitality properties. This advisor would be able to realistically value properties, recommend divestitures of individual hotels to make them more attractive, and could evaluate proposals and negotiate favorable terms on behalf of the government. To avoid any conflict of interest, the financial advisor should not be a potential buyer.

FLAG recommends awarding management contracts to international hotel firms. A management contract is a formal arrangement under which the owner of a hotel employs the services of an operator to act as his agent to provide professional management of the hotel in return for a fee. It will be necessary to trade some equity to entice professional management and gain the necessary capital for refurbishment.

Professional management will bring marketing strength, brand names, buying power, systems and procedures, project design and management, technical services, and training and management development. The selection process should be evaluated on the ability of the management firm to deliver a plan based on the above items and the level of investment in relation to the amount of equity demanded. It is essential to avoid speculators or firms without global reach.

Since most large hotel operators have a diversified portfolio of brands within their organization, those who are awarded management contracts for primary hotel properties could be also offered marketing franchises for lower category hotels.

To promote rapid development of quality tourism, specific hotels should be identified (see suggested List in Appendix B) and marketed to international hotel companies. The immediate goal should be one hotel in each resort. These hotels will act as anchors in the community and serve as a benchmark for the remaining hotels.

Once large tourist companies are re-organized according to core business, hotel category, and market synergy, individual hotels could be sold. To avoid real estate speculations, the land could be leased to investors for a period of 20 years. The State remains the owner of the land and is assured a long-term income stream from land rentals. The selling price for the Hotel could then be determined by the estimated current value of the building and PP&E, making the tender purchase

more attractive to potential investors. Tenders should be evaluated in view of the potential buyer's management plans to return the property to profitability and its commitment to invest.

To further capitalize on Montenegro's latent potential, an Investment Conference should be organized to attract international investors and operators for tourism projects. It should involve global hotel companies, developers, financiers as well as high governmental and diplomatic level officials from the EU and US. Various international financial institutions such as the European Bank of Reconstruction and the World Bank should also participate.

Montenegro also has the opportunity to participate in the International Tourism Infrastructure Conference in Athens, Greece on 1-3 December 1999. A large number of European and American companies are expected to participate.

Hotel Management

Privatization is the desired End State but the sale of 93 hotels will stretch over several tourist seasons. Directors and Managers of Hotel Companies should be retrained in Western Business Management and held accountable for sales and profits, for enhancing the hotel product image, and for protecting the value of the asset. To accomplish this they must:

- Use marketing techniques to drive revenues
- Improve customer service to the level expected
- Implement effective operating procedures to control costs
- Install financial controls and analysis according to the "Uniform System of Accounts" for Hotels

Performance of a management team should be compared to the best performance achieved in revenues and profits before taxes and depreciation within the Montenegro hotel industry at large. A monthly review and analysis of each hotel within each company should be conducted and each quarter the Ministry of Tourism should conduct a similar session with each hotel company.

Hotel managers must use all means available to them to drive business including Reservations Technology (Airline reservation system links -ACRS), Direct Sales, Sales Promotions, Public Relations, Advertising, Database Marketing/Direct Mail, and Travel Partners.

Hotels should link to a Computerized Reservation System (CRS) and establish the following rates to encourage travel agent bookings: corporate rates, travel consortium negotiated rates, package plan, season and off season rates, and special event rates.

In addition to seeking contracts with wholesalers and charter operators, hotel managers should identify and profile individual travel agencies in each major feeder market by special interests and then organize "City Promotions" in these markets.

REVIVING THE TOURISM MARKET

Target Markets

The Tourism Industry in Montenegro can serve the following international target groups:

- Art & Historical Societies, Cultural Heritage Foundations

- International Congresses, Meetings and Fairs
- International Incentives – Reward Tourism
- Family & Upscale Beach Tourism
- Nudist Beach Tourism
- International Athletic and Sport events
- International Hunting & Fishing
- Ski and Alpine Clubs
- International Diving, Rowing and Yachting Clubs
- Religious Tourism
- North European Senior Citizen Groups
- Regional Tour and Cruise Itineraries
- Adventure Tourism, rafting, hiking, mountain biking
- Ethnic Tourism
- Audubon Societies (Bird Watchers)

Proposed Sales and Marketing Strategies

Montenegrin hotel managers and tourist agencies must find creative ways to address the difficulties facing potential travelers with regard to booking travel to Montenegro, getting to Montenegro, and paying once they arrive

For the short term, it is wise to continue directing marketing and sales efforts toward Eastern Europe, KFOR, NGO and OSCE personnel and their families, and to “economy class” Western European Tour Operators

Open a sales office in Pristina, which should serve as the primary contact with local commanders, and as a liaison for Montenegro Hotels and Tourist Agencies marketing the special attributes of each tourist center

Hoteliers and Tourist Agencies must initiate contacts with former travel partners elsewhere in Europe in order to sign contracts for the Year 2000 summer season to place tourists into the hotels which still marginally satisfy the expectations of German, British and Scandinavian Tourists

Once Montenegro Airlines and other international airlines have established regular international connections, start an aggressive familiarization program for travel writers and travel agents from each target market

Organize an International Travel Fair in Montenegro in early spring 2000

Establish a joint Tourism website shared by the Ministry of Culture and the Tourism Promotion Agency. The website should be used to promote scheduled cultural events and festivals and should also have booking capabilities

Create, publicize, and promote an “Millennium Event ”

The Ministry of Sports should actively seek and promote international sport events to be held in Montenegro

The Hotel Industry should work with all types of charter operators such as advanced booking charters, one-stop charters, affinity group charters, multiple destination charters, travel group charters and group inclusive tours. Further, hotels must partner with retail travel agents and

airlines, offering the hotel product with excursion rates, advance purchase excursion fares (APEX), inclusive tours (IT), youth fares, and short-stay tour packages. This would require participation in Amadeus, Sabre, or another airline computerized reservation system.

VI OTHER RECOMMENDATIONS

National Park Service

In an effort to increase the number of visitors to National Parks, policies should be strictly enforced to control deforestation and defoliation, destruction of the eco-balance, trash, and pollution. To gain knowledge of new park management systems and techniques it is recommended that Montenegro

- Secure UNESCO membership for the Durmitor National Park
- Charge a mandatory entrance fee to provide funds and controls
- Organize a study trip for park managers to one of the best-managed US National Parks

Ministry of Culture

The Ministry of Culture plays a crucial role in the creation of an international image for Montenegro and in organizing events that will bring high profile travelers to the country. The following considerations are offered:

- Elevate the Herceg Novi Film Festival to the level of an international festival and create one additional cultural event of recognized European quality
- Actively pursue the establishment of production and distribution licensing law for domestically and foreign-produced films in Montenegro
- Produce a “great image” film to heighten the international appeal of Montenegro (similar to the “Sound of Music” for Salzburg)

Ministry of Agriculture

Agricultural products produced in Montenegro meet most of the requirements for the Tourism Industry. This leverages tourism income. For future considerations, the following actions are suggested:

- Encourage agricultural associations to produce attractively packaged “branded” cheese, prsut (smoked ham), olive oil, and wine for tourist export
- Make the dairy industry self-sufficient by seeking a foreign partner to build a modern dairy plant that produces a wide range of products for hotels, restaurants and specialty shops (ice cream, yogurts, small packaged creams, etc.)
- Seek a foreign partner to build a fruit processing and packaging plant for products to be used in hotels, restaurants, and export shops (e.g. individual packaged juices and marmalades – such as the Swiss brand HERO products)

Ministry of Education

The Ministry of Education plays a critical role in educating hotel managers for the transition to a market economy and in training the employees who will create the best “hospitality experience”
The following proposals are offered

- Link the KOTOR Hotel and Tourism College to an American/European Hotel school to provide a mechanism for cross training of teaching staff and for visiting professor programs
- Seek Membership in CHRIE - Council for Hotel & Restaurant Industry Education
- Include Travel & Tourism Research in the Faculty of Economics at the University
- Include a travel agent training program at the Tourism College
- Provide opportunities for honor student to study abroad
- Provide Hospitality Management education at the University Level including hotel accounting and financial management, sales & marketing management, hotel technology and MIS (Management Information Systems), engineering and property management, and real estate management

Ministry of Transport

The Ministry of Transport provides the crucial link for tourist movements to, from, and within Montenegro. The following proposals are offered

- Implement the strategic plan to complete the Sozina Tunnel (Podgorica to Bar) and other planned road improvements
- Upgrade the Bar to Berane Train with the panorama-type tourist coaches used in the European alpine regions
- Upgrade the Podgorica and Tivat Airports to international standards and complete the Durmitor and Berane airfields
- Add hydrofoils for the Bar – Bari Sea line

“Morsko Dobro” Coastal Management

This agency plays a vital role in reversing the trend of unplanned beach development and preserving the coastline for Montenegro citizens and for visitors who contribute to the economy. As priorities, the following actions are suggested

- Preserve the beaches in the Milocer/ Sveti Stefan area for the upscale tourist market
- Accelerate the program of leasing beachfronts to private entrepreneurs
- Allow only upscale developments such as executive resort condominiums, golf resorts, yacht harbors with executive residences, etc
- Consolidate all community development plans under the control of Morsko Dobro or another appropriate agency to assure implementation of a Master Plan that will meet the public interest for preserving and improving the coastal zone

VII PRIORITIES FOR PLANNED DEVELOPMENTS

Montenegro is over-capacity in current hotel facilities. The major thrust for available capital should be to renovate and upgrade existing facilities -- particularly those that occupy prime locations. However, several opportunities do exist for construction of new facilities that will widen opportunities for visitors. Golf is becoming more popular in Europe, and a golf facility is essential in attracting both a large segment of individual travelers and the business/conference market. Golf

signifies a high level of sophistication to many upscale travelers and is linked in their eyes with quality tourist offering. In addition, carefully developing prime locations with quality resort type condominiums will also attract capital. Marinas, sport complexes, and mountain ski resorts are other possibilities. The following list suggests opportunities for such investment:

- Golf Club and Resort in Igalo / Sutorna Valley
- Golf Club & Resort with Executive Villas – in Buljarica
- Golf Club & Conference Resort in JAZ
- Golf Club & Conference Resort in Zabljak
- Executive Villa Resort Development plus tennis in Tivat / Zupa
- Further development of four-season mountain resorts
- Sport Hotel Development at Kolasin Ski slopes
- Hotel Marina Resort in Meljine

VIII CONCLUSIONS

The majority of the key tourism leaders recognize the challenges facing the industry. The assessments identified in this report echo the sentiments of most tourism professionals. The recommendations presented are similar to those in earlier studies. People working in individual sectors of the tourism industry often reveal a passive attitude since solutions are above their level. Success in unlocking the potential of the tourism industry is not the sole responsibility of the Ministry of Tourism. Comprehensive action from a variety of ministries and both state owned and private companies is required. Resources must be invested in creating an alluring image. Privatization can attract direct foreign investment that will provide both management skills and capital. Diplomatic efforts are required to reestablish international air access and land transfers from Croatia. A healthy banking industry is required to provide financial services for travelers and to provide capital for local entrepreneurs. Montenegro must abandon a “one size fits all” marketing approach and segment the market. Hotel managers and other key figures must realize that marketing is not the sole responsibility of the government. If the recommendations in this report are implemented the tourism industry will significantly increase its contributions to the economy of Montenegro.