

ENTREPRENEURIAL FRAMEWORK CONDITIONS FOR THE SME DEVELOPMENT IN SERBIA*

CHAPTER

9

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Abstract

The SME development in Serbia, like in the most of the Western Balkans countries, shows a significant improvement. Serbia has adopted the SME development policy which is in accordance with the EU policies and is actively engaged on improvement of the business environment in order to foster the SME further expansion. It has moved from the phase of formulating policy and defining strategic objectives to implementing policy, particularly in the field of start-ups, provision of business services and dissemination of information. Analysis of the current framework conditions for the SME sector, and its role and significance, demonstrate considerable enhancements in transition period. However, SMEs in Serbia still face numerous problems, that this sector encounters in its business operating. The analysis of business environment for SMEs in Serbia has been performed through consideration of poll survey Global Entrepreneurship Monitor (GEM) as well as annual reports „SME Policy Index 2007” and „SME Policy Index 2009” which show realized progress in application of the European Charter for Small Enterprises in the Western Balkans with special emphasis on Serbia. The most important findings in the paper suggest that, despite realized progress, business environment in Serbia is still under-stimulating for SMEs development due to certain limitations of legal, procedural and financial nature, whereby defined recommendations for improvement of framework for business operating of SMEs in Serbia have been formulated.

Key words: Serbia, small and medium enterprises (SMEs), SMEs development, TEA Index, SMEs policy index.

INTRODUCTION

The majority of Western Balkan, understanding the importance of the small and medium enterprises (SMEs) and streaming to join the EU, have formulated their national SME development policies and created the programs and strategies for this sector. These countries pay significant attention to SMEs, considering it of great importance, because the development of this sector presents the remarkable part of overall economic reforms directed to creation of market economy.

The European Charter for Small Enterprises, as the document of the European Commission, which governments of the countries of the Western Balkans adopted in 2003, represents the main instrument for promotion of policy of entrepreneurship and small enterprises. In June 2008, European

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Commission adopted the „Small Business Act“ for Europe, which was confirmed in December 2008 by Council of Europe. Realized progress in the application of implementation of the European Charter for Small Enterprises has been presented in annual reports. By signing this Charter on June 21, 2003, Serbia has committed to work in accordance with ways of action that are valid in European Union, taking into consideration needs of small enterprises.

In the last several years, conditions for business operations of SME in Serbia were improved. Serbia has traversed very quickly from the phase of formulating policies and defining strategic goals into the phase of realizing policies, especially in fields as the support to innovative and start-up enterprises, providing business services and dissemination of information via on-line services, as well as the improvement of dialogue on SME policy between public and private sector. However, business operations of SME sector in Serbia during the preceding period were followed by numerous problems, starting from those regarding administrative barriers, through difficult access to finance sources and insufficient financial support of the state, till the impact of the world financial crisis and chronically present high level of grey economy.

This paper consists of three major parts. First, the current state of SME sector development in Serbia, its role and significance, as well as the main problems it encounters in its business operations were analyzed. After that we examine business environment for SMEs in Serbia through the analysis of poll survey Global Entrepreneurship Monitor (GEM), as well as annual reports „SME Policy Index 2007“ and „SME Policy Index 2009“ which show realized progress in the application of the European Charter for Small Enterprises in the Western Balkans. Finally, in a conclusion, the most important findings in this paper and formulated defined recommendations for additional improvement of framework for business operating of SMEs in Serbia will be presented.

CURRENT STATE OF SME SECTOR DEVELOPMENT IN SERBIA

SME sector is becoming more and more important for Serbian economy. The reinforcement of SME sector role in the transition period is, at the first place, the result of general business environment improvement and enhancement measures undertaken by the all administration levels. Accordingly, the development of the SME sector in Serbia has favorable trends, regarding the growing number of these enterprises, the number of employees, the overall turnover, and, finally, the profitability level.

Dynamic analysis of the level of development of SME sector reflects continuous increase of influence of this sector on the development of economy in Serbia. In this sector the number of employees has been growing, turnover has increased, as well as gross value added (GVA) and exports. During the course of 2005 to 2008 SMEs participated approx. 99.8% in a number of business organizations, 63.7% in the employment rate, 66.8% in turnover and 57.1% in gross value added of the non-financial sector. In Serbia 303,449 SMEs and entrepreneurs are engaged in economic activities, which employ 940,159 people and make 66.6% turnover and 59.1% gross value added in non-financial sector of economy. Details are presented in the table which follows, having in mind that it contains only the data on the number of registered SMEs and entrepreneurs. The number of SMEs is smaller and does not surpass the number of 100,000.

Achieved results in SMEs sector contributed greatly to the improvement of efficiency of economic operations in Serbia in general. This sector proved the most profitable and the most competitive part of Serbian economy, having achieved net income, influencing improvement of business efficiency of the whole economy. The profitability rate of SME sector was considerably high and amounted to 58.7%. The comparative advantage of SME is its flexibility, its fast adaptation to changes and its possibilities in satisfying the fluctuate market demands. Additionally, the low fixed costs present important baseline and comparative advantage of these enterprises. Simultaneously, the great number of these firms is characterized by innovativeness, entrepreneurship initiative and creativity, which is of remarkable significance for the accelerating technological development.

Table 9.1. Level of SMEs Sector Development

	SME + Entrepreneurs				Participation of SMEs and Entrepreneurs in Economy in %			
	2005	2006	2007	2008	2005	2006	2007	2008
Number of companies	276,695	268,515	296,086	303,449	99.7	99.8	99.8	99.8
Number of employees	810,862	870,979	906,669	940,159	59.0	63.1	65.5	67.2
Turnover, bn EUR	34.98	45.29	51.83	57.3	65.5	67.5	67.6	66.6
GVA, bn EUR	5.89	7.47	9.09	10.3	54.1	56.9	58.3	59.1

Source: Serbian Agency for the Development of Small and Medium-sized Enterprises and Entrepreneurship

This sector has played important role in opening of new jobs in period from 2004 until 2008, when the number of job was downsized for 163,620 due to the restructuring of economy, but 187,419 workers were employed in SME sector in the same period.

But in spite of achieved results, the current state of SME sector development in Serbia is far from desirable. When Serbia is compared to EU by density of SMEs per 1,000 inhabitants, the indicators are fairly favorable. Serbia is at a level of EU average with 41 SMEs per 1,000 inhabitants. However, there are big differences in EU by individual member countries – Czech Republic, for example, has even 91 enterprises per 1,000 inhabitants.

The main issues in business operating of SMEs are administrative barriers, like tax procedures, obtaining building permits and registration, economy, collection of receivables, insufficient coordination of operating with quality standards, elevating competitiveness, better solving of issues regarding lack of workers with adequate professional qualifications ...

The access to finance sources is one of major, if not the biggest challenge for development of SME sector in Serbia. High interest rates on loans and conditions for provision of loans present, very often, insurmountable obstacle for entrepreneurs.

Furthermore, the impacts of the world financial crisis, as well as high percentage of grey economy in Serbia have strong destructive effect on SMEs current state. Last, but not the least, the inadequate state support has also restrictive effect on the development of this sector.

BUSINESS ENVIRONMENT FOR SME DEVELOPMENT

By the establishment of macroeconomic stability, implemented reforms and institutional changes in the last several years, conditions of business operations of SME on Serbia were improved to a certain extent. Many of the eligible international researches confirm that progress.

Global Entrepreneurship Monitor (GEM) - A large progress in comparative consideration of entrepreneurial activity is represented by poll survey of Global Entrepreneurship Monitor (GEM) which has followed the development of entrepreneurship in its initial stage, as well as motives of engaging in entrepreneurship. The purpose of this empirical research (the smallest sample by countries was 2,000 respondents within adult population), is the creation of a base for formulating and conducting efficient policy of encouraging the development of entrepreneurship.

For determining the TEA index (Total Early Entrepreneurial Activity), two indicators are defined, by which the presence of entrepreneurship in early stages of development of a company is expressed:

- TEA Beginners (individuals who started up the procedure of establishing new enterprise or deal with new business, as well as self-employed, who have been paying salaries three months at the most);
- TEA New entrepreneurs (individuals employed as owners/managers of new enterprises who have been paying salaries 3 months at the least, and 42 months at the most).

TEA index for Serbia was 7.6 in 2008, which means that on each 100 adult persons almost 8 were active entrepreneurially, and 9 persons have continued to operate longer than 42 months. Initiated process of structural reform has crucial impact to intensive entrepreneurial activity of Serbia, and in the first place, the privatization of socially-owned enterprises and restructuring of large systems, where the rationalization of the number of employees is one the key measures of economical-financial consolidation of enterprises.

High rate of early entrepreneurial activity in Serbia coincides with basic results of GEM research - early entrepreneurial activity has been expressed in all countries with low income, countries in transition with high unemployment rate, where the population in most cases, determined for entrepreneurial activity forced by the situation in which they found themselves. With the development of institutions and growth of national welfare and overall standard, the rate of early entrepreneurial activity falls down. The researches and results of GEM show that when countries reach relatively high level of GDP, the greater are the possibilities for development of, whereby motives to start-up business are different qualitatively (more focused to spotting business opportunities, and less to entrepreneurship in need).

The results of GEM research show that the development (especially early) of entrepreneurship in Serbia, although intensive, has been burdened by numerous developmental limitations specific for countries in transition. By intensifying structural reforms, stopping the outflow of young and professional staff, forming certain institutions for support, education and other forms of assistance at own business start-up, the growth of entrepreneurial activity can be, in next period, achieved. That involves faster harmonization of legal and economic system with EU as essential condition for further overall sustainable development, and by that also creating favorable climate for faster development of entrepreneurship.

The SME Policy Index by monitoring and evaluating the progress in implementing the main policy framework for small and medium-sized enterprise development (elaborated by the European Union: The European Charter for Small Enterprises) is an essential benchmarking tool that for examine the policy effectiveness towards SME. The SME Policy Index uses collaborative benchmarking to measure progress in the ten dimensions of the Charter:

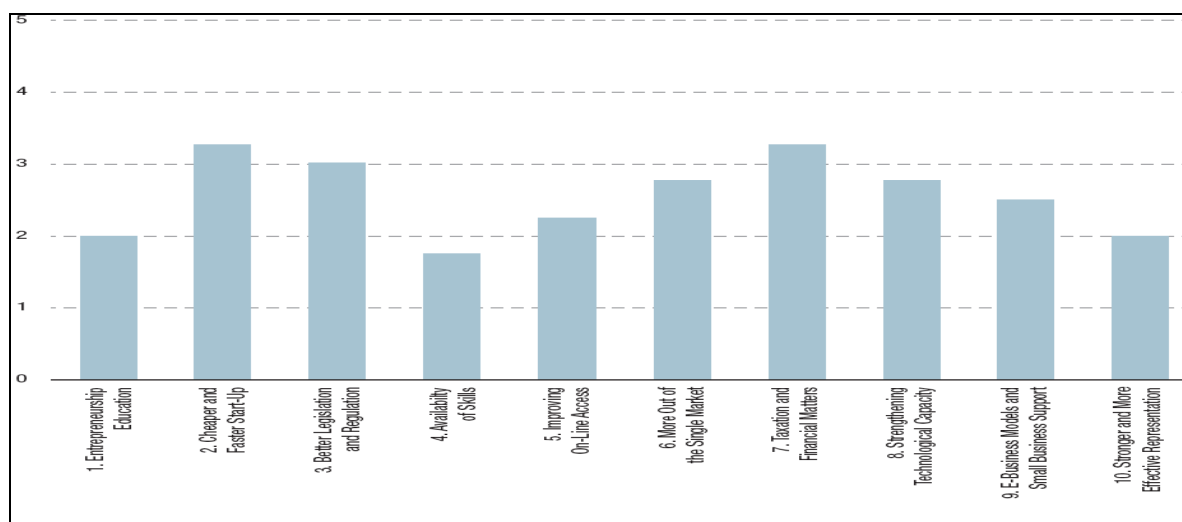
- Education and training for entrepreneurship;
- Cheaper and faster start-up;
- Better legislation and regulation;
- Availability of skills;
- Improving online access for tax filing and company registration;
- Getting more out of the single market;
- Taxation and financial matters;
- Strengthening the technological capacity of small enterprises;
- Successful e-business models and top class business support;
- Developing stronger, more effective representation of small enterprises.

In the SMEs Policy Index, each dimension has been broken down into sub-dimensions. These sub-dimensions have then been divided into qualitative and quantitative indicators of policy development, on a scale of 1 to 5. The lowest level (1) indicates a lack of policy initiative. The highest level (5)

denotes implementation that is close to good practices, as defined by the Charter implementation process at pan-European level and the OECD SME Bologna Process.

According to the Report on the Implementation of the European Charter for Small Enterprises in the Western Balkans (2007) Serbia has established a solid policy framework for the development of SMEs with overall average SMEs Policy Index between 2 and 3 (2.48), similarly to the Former Yugoslav Republic of Macedonia and Montenegro.

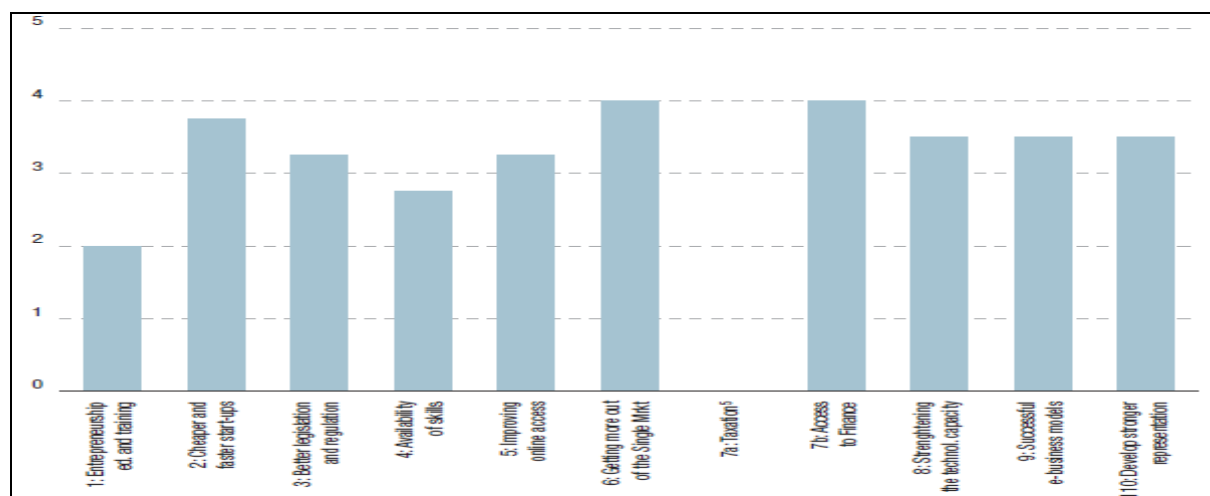
Figure 9.1. SME Policy Index scores for Serbia per Charter dimension 2007



Source: OECD (2007), Progress in the Implementation of the European Charter for Small Enterprises in the Western Balkans: 2007 SME Policy Index, Paris

The 2009 report (Figure 9.2.) shows that there have been significant changes in policy developments in Serbia across a wide range of dimensions. Serbia was rated in this cycle with overall rate 3.3 (on the scale of possible 5), which is significant progress compared to last round (2.48).

Figure 9.2. SME Policy Index scores for Serbia per Charter dimension 2009



Source: OECD (2009), Progress in the Implementation of the European Charter for Small Enterprises in the Western Balkans: 2009 SME Policy Index, Paris

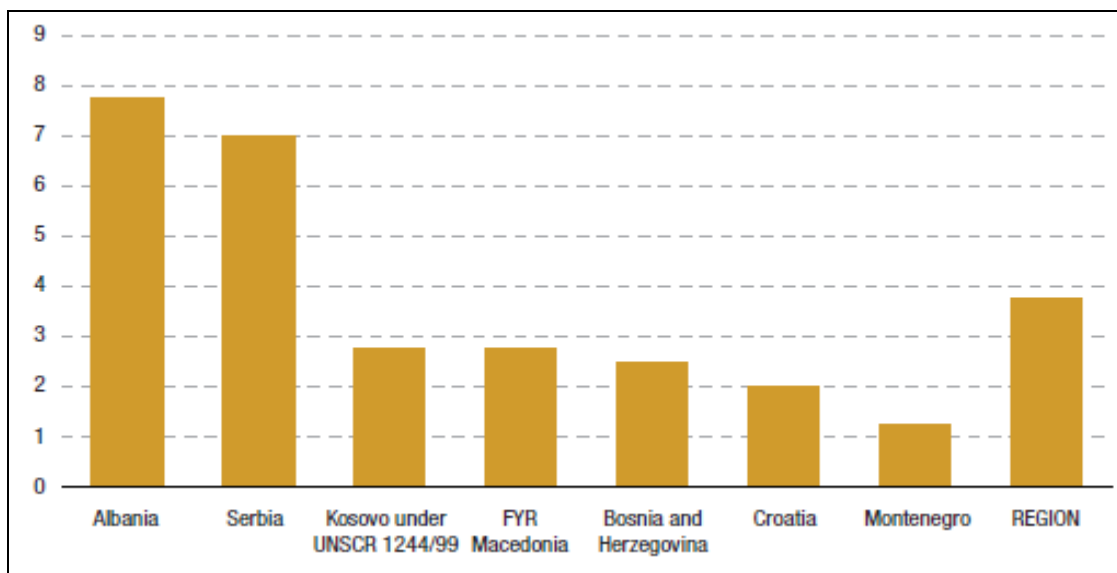
Serbia has moved rapidly from the phase of policy elaboration and definition of strategy objectives to policy implementation in areas such as support to innovative companies, start-ups, provision of business services and information dissemination through online services. It has significantly improved its record on public-private policy dialogue. In addition, Serbia has improved its performance, in an incremental way, in a number of areas where it already had a positive implementation record, as in company registration and export promotion. Serbia is evaluated favourable concerning faster and not so expensive business establishment, legislative improvements, SME taxation and financing and also technological capacity building. However, Serbia is lacking behind the other Western Balkans countries concerning entrepreneurship education and training, e-business, skills and knowledge necessary for SME development, SME support within the public sector.

The most significant measures of institutional support, which have contributed to the improvement of conditions for business operations of SMEs in Serbia, were:

- Within the context of improvement of conditions for business operations of SME and entrepreneurship, the Strategy of Regulatory Reform in the Republic of Serbia in period 2008-2011 was adopted, by which overall reform of regulations is anticipated, the effects of which will be reflected in decreasing regulatory burden for SME, with expectations for administrative costs of operating to be reduced for 25% at least until 2011;
- Financial support was realized in following ways: grants, long-term loans under extremely favorable terms for business start-up, support of SMEs development in the most undeveloped municipalities, loans for encouraging the quality of catering services of physical persons, as well as SMEs from the field of tourism, then encouraging promotions of exporters, financing SMEs export, export insurance and issuance of guarantees for loans to SME. The realization of mentioned support was implemented through institutional infrastructure, which was mainly formed in preceding years. Key role in the realization of credit support under favorable terms had the Development Fund of the Republic of Serbia and the Export Credit and Insurance Agency of the Republic of Serbia. As a support to SMEs in 2008, it was allocated to them from the budget of the Republic of Serbia around EUR 136.9 mln and from the sources of the Development Fund of the Republic of Serbia loans in amount of around EUR 102.5 mln were approved, so that overall provided support to SME sector amounted to around EUR 239.4 mln EUR;
- Financial support to forming of incubators is continually provided, as the instrument of local economic development and realization of innovative projects;
- By bringing the Strategy of development of competitive and innovative small and medium enterprises for period 2008 until 2013. (where one of the pillars is just connected to finance and taxation of SME), directions of action were practically determined on the segment of financial support and development of financial market, which would have to be more directed SME sector, because several institutions currently exist, which provide financial support to the sector, whereby coordination and cooperation is present, the scope and quality of which is still at unsatisfactory level;
- With aim to mitigate administrative burdens, following measures of institutional support were undertaken: since February 2008, period required for registration ea reduced to 24 h for entrepreneurs and 28 h for business subjects; the procedure of electronic registration of entrepreneurs was introduced, by which satisfactory effects, however, were not realized (formalization of business start-up still requires 11 procedures and 23 days, which classifies Serbia far behind the OECD countries);
- With aim of encouraging the internationalization of SME, besides activities on promotion of export, the Project to support cluster development of Serbia in 2008 was also implemented, and in addition to that positive effects were also realized in the field of human resources and improvement of the level of knowledge and capability of entrepreneurs, owners of SME and employees.

For illustrative purposes of progress of the Western Balkans countries (and especially of Serbia) in the implementation of the European Charter for Small Enterprises after 2007, we shall use next figure.

Figure 9.3. Overall cumulative changes in scores - 2007 to 2009 SME Policy Index in the Western Balkans



Source: OECD (2009), Progress in the Implementation of the European Charter for Small Enterprises in the Western Balkans: 2009 SME Policy Index, Paris

The SME development in Serbia shows that there has been a significant improvement in business environment and SME development in the county. Serbia has adopted the SME development policy which is in accordance with the EU policies and it is actively engaged on improvement of the macroeconomic measures in order to foster the SME further development.

CONCLUSIONS AND RECOMMENDATIONS

Macroeconomic stability, the reforms in juridical system, tax system, customs system, as well as in the procedures regarding starting a business are evaluated to have a positive impact on business environment. It is reported that the most significant changes are made in the procedures related to starting a business, getting credits (through guarantee fund establishment, start-up support, exports and innovations), also by organizing different agencies on national and regional level the small and medium-sized business is being facilitated. Furthermore, the improvement has been made concerning protecting the investors by adoption of new law on bankruptcy proceedings. On the other hand, there are still missing the improvements in the field of entrepreneurship education, e-business, cluster establishment, access to foreign markets, as well as in the administrative regulation and institutional infrastructure.

Despite the realized progress, business environment in Serbia is still assessed as under-stimulating, and possibilities for faster SMEs development in Serbia have not been sufficiently exploited, due to certain limitations of legal and procedural nature, and in comparison with EU member countries, but also in some countries in surrounding, SMEs in Serbia are considerably more burdened by administrative procedures. The improvement of factors which influence the provision of access to finance sources of SMEs is evident, which is reflected through following: The system of credit guarantees has been improved in direction of widening their scope, the Register of pledges on movable property and rights by the Agency for Business Registers has been established and it is completely operative, functioning of the register of data on liabilities of legal entities and physical persons though

Credit Bureau is provided, significant progress has been made on introducing of the system real estate and establishing legislative regulations which are essential for functioning of investment funds.

The level of knowledge and capability of entrepreneurs still lags significantly behind needs of creating competitive, export oriented SME sector. The reform processes directed towards overcoming this state have been initiated, but they require longer period of time. The access of SME to finance sources is still limited to a great extent. The pole of finance of SME sectors is still represented the Fund Development Fund of the Republic of Serbia, through which incentive credit lines of the Ministry of Economy and Regional Development are realized by special programmes. Bank loans are still very expensive and inaccessible to the biggest part of interested SME.

We consider that it is very important that European Union should make regulations more often, which would create favorable ambient for development of SMEs and insist for such elements to be included in Serbian legislation regarding the development of SMEs, because Serbian SMEs have small capital, and the financial support of the state is modest and insufficient. The access to finance sources is, among others, one of the biggest challenges for development of SME sector in Serbia. High interest rates on loans and conditions for provision of loans often represent insurmountable obstacle for entrepreneurs. Should the impact of the world financial crisis be added to that, as well as exceptionally high percentage of grey economy in Serbia and its destructive effect on SMEs, it can be freely said that our SMEs are in fairly difficult situation.

In addition, future entrepreneurs in Serbia encounter numerous problems, among which the time required for getting permits and licenses are particularly pointed out (during application of the laws entrepreneurs encounter difficulties which are not caused by the quality of legal provisions, but procedures for their implementation. It is to be expected that many of these problems should be solved by announced abolition of unnecessary regulations, but also by elevating knowledge level of entrepreneurs through introducing entrepreneurship in educational system, strengthening credit support in investment, investing in small and middle enterprises in undeveloped regions, as well as work elevating the level of competitiveness and innovativeness of SMEs.

Some of recommendations for improvement framework of business operating of SMEs in Serbia could be following:

- Creating favorable entrepreneurial framework conditions for the SME development;
- Providing necessary education for entrepreneurs whereby the institution for training should provide adopting of adequate knowledge and skills, adapted to needs of small enterprises, as well as to include forms of learning throughout whole life (a life-long learning);
- The promotion of online access (in communication between enterprises and state administration) and introducing of electronic access to governmental services with on-line services adapted to small and middle enterprises;
- Faster and simpler establishing of enterprises (the possibility of online registration of companies) and development of the model of electronic business operating and efficient support to small enterprises;
- More efficient legislation and more efficient representation of interest of small enterprises at professional and national level;
- The development of entrepreneurial culture and creation of environment that is stimulating for development of small and middle enterprises;
- Strengthening of dialogue and partnership between public sector and small and middle enterprises sector
- Corporate networking, improvement of cooperation among the Government, private sector and entrepreneurs is one of the prerequisites for economic development;
- Creating business environment that stimulates investments and competition and enables operating of different enterprises and industries, as well as special social and economic programmes in Serbia.

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