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# Key Findings and Conclusions

## Overview of the European Charter for Small Enterprises process in the Western Balkans

This report presents an assessment of the quality and the level of implementation of small and medium-sized enterprise (SME) policy in the Western Balkans, comparing results with a previous assessment conducted in 2006 and published in 2007. The report covers Albania, Bosnia and Herzegovina, Croatia, the former Yugoslav Republic of Macedonia, Montenegro, Serbia and Kosovo under UNSCR 1244/99.

The assessment framework is based on the European Charter for Small Enterprises (the Charter), a set of policy guidelines endorsed by the European Union Member States and a key component of the European Union Lisbon Agenda. The Western Balkans governments adopted the Charter in 2003 and in 2006 launched a three-year assessment process for the Western Balkan region, which was completed at the end of 2008.

In June 2008 the European Commission adopted the Small Business Act, a new framework policy document for SME policy including policy guidelines as well as targeted actions to support SMEs. The document was endorsed by the European Council in December 2008. The Western Balkans countries and Kosovo under UNSCR 1244/99 are expected to move towards implementation of the policies identified in the Small Business Act.

This report assesses the implementation of the European Charter for Small Enterprises in the Western Balkans and has been jointly elaborated by the European Commission (EC), the European Training Foundation (ETF), the European Bank for Reconstruction and Development (EBRD) and the Organisation for Economic Co-operation and Development (OECD). It is based on data and information collected over a six-month process, with a cut-off date of 15 November 2008. As in the case of the 2007 report, the report presents a synthesis of two parallel assessment processes: a self-evaluation conducted by the Western Balkan governments and co-ordinated by the national Charter co-ordinators; and an independent evaluation conducted by the four partner organisations, with inputs from the private sector and other SME stakeholders.

The report covers the ten policy dimensions included in the Charter. It applies a methodology known as the SME Policy Index, which makes it possible to quantify and compare qualitative policy features. Each dimension has been broken down into a set of sub-dimensions and into a number of analytical policy indicators. Each indicator is based on a five-step policy development path ranging from a level 1 (lack of policy initiative) to a level 5 (implementation close to the good practices from the EU Member States collected in the Charter and in the OECD SME Bologna Process). The set of analytical indicators used in the 2009 report is not significantly different from the set used in the 2007 report, with the only exception of the sub-dimension on tax policy, securing a good level of comparability between the two assessments.

The report is organised in three parts. Part I covers a review of progress by policy dimension. Part II, elaborated by Professor Stephen Roper from Warwick Business School, University of Warwick (UK), focuses on policies supporting high-growth SMEs. The intention is to provide a comprehensive review of good practices, introduce country assessment methods through two case studies (the former Yugoslav Republic of Macedonia and Serbia) and open a debate on what is likely to be a key component of the SME agenda for the next few years. Part III includes stock taking and progress reviews for each of the seven Western Balkan economies.

## Key findings on progress in policy elaboration and implementation at the level of the Western Balkan region

The key finding of the 2009 report is that over the last two years there has been good progress in elaborating and implementing policies supporting small enterprises all across the Western Balkans and there is clear convergence towards the adoption of the policy guidelines set in the Charter. However, progress has been uneven across the ten dimensions and the seven economies covered by the report.

In particular, the Western Balkan governments have made generally good progress in the policy areas that directly affect the operational environment for small

enterprises. For instance, the company registration process has significantly improved in terms of time, costs and steps required across the Western Balkans, with the only exception of Bosnia and Herzegovina. A wide range of regulatory reform programmes have been launched and are currently implemented in most of the Western Balkan economies. The credit environment and the range of financial products available to SMEs have also improved.

On the other hand, most of the Western Balkan governments are at a relatively early stage in introducing targeted policies for relevant types of SMEs, such as start-ups, export-oriented and high-growth companies. For instance, few governments have introduced measures targeting start-ups (positive examples are Croatia and Serbia), targeting innovative enterprises, or supporting technological or non-technological innovation.

Even in the cases where policies have been formulated and specific measures have been introduced, as in the cases of Croatia, Serbia and to a lesser extent the former Yugoslav Republic of Macedonia and Albania, the amount of available resources is still a fraction of what is available for instance in the new EU Member States. Most of the programmes launched in the areas of technological export promotion or competitiveness either do not reach the critical level to have a positive impact on company behaviour, or are structured in a way that fails to generate positive synergies with other measures.

The contribution of human capital to enterprise performance remains a particular constraint to the economies of the region. More effort is required to ensure that education and training is strategically knitted into the wider competitiveness drive within each country. Enterprises, in partnership with the public sector, will need to assume more responsibility in defining training requirements and ensuring that these are systematically articulated to the training market. Further, better recognition of EU recommendations for promotion of entrepreneurship at all levels of education is required, with particular emphasis on entrepreneurship promotion in early education.

The Charter assessment cycle completed over the last two years (2007-2009) offers a good picture of the challenges faced by policy makers in engineering and steering reforms in the SME policy area. It also points to some of the key elements that are underpinning policy reform. The 2009 report shows that a two-year policy horizon can be sufficient for elaborating and implementing policy reforms with clearly defined objectives that can be

monitored. These reforms should have relatively limited state-budget implications and involve few institutional and legislative changes. Implementation can be delegated to executive agencies and approaches can be modelled on existing good practices.

However, reforms take place only if government provides strong political backing, secures the consensus of the stakeholders, ensures good planning and effectively manages external technical assistance.

Good examples in the region are the successful restructuring of the company registration process in Albania, which has introduced a state-of-the-art registration system in less than two years, and the launching of the one-stop system in the former Yugoslav Republic of Macedonia. A negative example for the same area is the stalling of company registration reform in Bosnia and Herzegovina, under consideration since 2003.

Other more complex reforms that call for institution building, extensive inter-ministerial co-ordination and legislative changes (and have wider budget implications), such as those related to human capital development and regulatory reform, require longer elaboration and implementation time, hence a five-year horizon is more common. Policy development moves along the path defined in the assessment framework, starting often with pilot projects as a first response to perceived policy needs, before moving to the elaboration of a policy strategy. Then there are changes in the institutional and legal framework, the establishment of new policy institutions and finally, the beginning of the implementation phase.

A tool such as the SME Policy Index assists governments in identifying key policy priorities and building consensus around policy reform.

## Progress at country level

The 2007 report divided the Western Balkan economies according to the level reached in terms of policy performance.

A first group, made up of Albania, Bosnia and Herzegovina, and Kosovo under UNSCR 1244/99, was characterised by a level of performance across the ten dimensions around level 2, denoting an institutional and legal framework underpinning SME policy still largely reliant on *ad hoc* intervention and pilot projects, and in need of further concretisation.

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A second group, made up of the former Yugoslav Republic of Macedonia, Montenegro and Serbia, described countries that had largely completed the legislative and institutional framework supporting SME policy and had just entered into the phase of policy implementation. Their performance level was between level 2 and level 3 in most dimensions. Finally, Croatia was highlighted as the most advanced country in terms of SME policy.

The 2009 report confirms Croatia as the region's most advanced country in terms of SME policy elaboration and implementation in the Western Balkans. In each policy, excluding the human capital dimensions and tax policy, Croatia has recorded a performance well above level 3. Three policy dimensions (Getting more out of the Single Market, Successful e-business models and top-class business support, and Improving online access) indicate that a sound policy framework is in place and the country is moving ahead particularly well with policy implementation. Looking at the analytical indicators, policy improvements seem widespread, but incremental. No major policy initiatives have been launched over the last two years, as the country has been focusing on the implementation of existing policies and on the completion of the EU accession process.

The 2009 report shows that there have been significant changes in the dynamic and the composition of the second group. There have been significant policy developments in Serbia across a wide range of dimensions. The country 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.

There have been limited improvements in the overall performance of the former Yugoslav Republic of Macedonia and Montenegro: few policy initiatives have been launched over the last two years. Both countries have made significant progress on two dimensions relating to human capital development and, to a lesser extent, on the provisions of business support services. However, they are relatively weak in the key areas of supporting SME competitiveness and technological capacity, as well as in the export promotion area.

Albania's policy performance over the last two years has been remarkable and has allowed the country to join the second group. Albania's record of policy implementation has improved in all ten dimensions; in particular, in all the policy areas linked to the general operational environment (such as company registration, regulatory reform, access to finance and export promotion). The weak points in Albania's performance remain human capital development and technological capacity of SMEs.

The 2009 report shows that there are two economies in the region that, for a variety of reasons, are still in a phase of completing the basic institutional, legal and regulatory requirements underpinning SME policy: Kosovo under UNSCR 1244/99, and Bosnia and Herzegovina. However, while the former has shown significant progress over the last two years, SME policy implementation in Bosnia and Herzegovina has largely stagnated. Inside Bosnia and Herzegovina, there have been differences in performance across the two entities (the Federation of Bosnia and Herzegovina, and the Republika Srpska) and the District of Brcko. Progress has been more marked in the Republika Srpska, which is engaged in a comprehensive regulatory reform and has an active policy towards the small enterprise sector conducted through the entity SME Development Agency, and in the District of Brcko.

In Kosovo under UNSCR 1244/99, there has been progress on the institutional front, with the establishment of an SME Development Agency, the assignment of the export promotion task to the Investment Promotion Agency, and the improvement of the legal and regulatory framework related to access to finance. The provision of services to SMEs is still performed mostly through donor-funded projects, as the newly established SME Support Agency is still building capacity and developing its own tools. Kosovo under UNSCR 1244/99 has additionally developed a good lifelong entrepreneurial learning strategy with a range of institutional partners having signed up to its implementation.

In Bosnia and Herzegovina there is still room for progress in the SME policy area at state level. Policy elaboration and implementation is highly decentralised, with the two entities and the district of Brcko having direct responsibility for most of the ten policy dimensions covered by the Charter. In addition, the ten cantons in the Federation of Bosnia and Herzegovina have legislative and regulatory powers in SME policy areas, while the five local development agencies play a stronger role in SME support.

**Table 1**

## Key SME policy reform initiatives launched in the Western Balkans since the 2007 SME Policy Index Report

<b>ALB</b>	<p>Over the last two years, Albania has radically reformed the company registration process, with the financial and technical support of the US-sponsored Millennium Challenge Corporation, and co-ordinated by the Ministry of Energy, Economy and Trade. The reform is remarkable for its scope, its speedy implementation and the quality of the results. The starting point of the reform process was the passing in May 2007 of the Law on National Registration Centre (NRC) that transferred competence over company registration from the Tirana court to a new dedicated public agency. In the year after the establishment of the NRC, there has been a significant surge of new company registrations, surpassing the threshold of 15 000 new applications. The centre is also updating the records of existing companies, including those records in the new electronic register. It is processing the large backlog of company record modifications accumulated under the previous system.</p>
<b>BIH</b>	<p>The definition of collateral is encouragingly flexible in Bosnia and Herzegovina and micro-loans can be extended in the absence of collateral. USAID sponsored a project to set up a registry for movable assets, which became operational three years ago, on a state-wide basis and regulated by a state-level law. In this registry anyone who is in Bosnia and Herzegovina can enter information about pledged movable assets. A credit registry exists and is well functioning, although individuals' access to their own credit data is not guaranteed by law.</p>
<b>HRV</b>	<p>Croatia has been the first Western Balkan country to rigorously tackle competitiveness issues amongst SMEs. BICRO, the Business Innovation Centre of Croatia, plays a central role in supporting innovative SMEs: it runs a number of programmes, ranging from R&amp;D support to equity financing. The Koncro programme strengthens the technical and managerial skills of innovative SMEs, through the co-funding of consultancy services. Meanwhile, the institutional support for promoting entrepreneurship key competence by the National Curriculum Council and education authorities provides an important basis for mainstreaming entrepreneurship promotion in formal education. Finally, the Croat-led project to establish a South East European Centre for Entrepreneurial Learning demonstrates good initiative and further commitment to regional co-operation.</p>
<b>XK</b>	<p>Kosovo under UNSCR 1244/99 has established the SME Support Agency, which is the responsible institution for the elaboration of SME policy and its implementation. The agency's responsibilities include:</p> <ul style="list-style-type: none"><li>• Developing a policy framework supportive for SMEs</li><li>• Initiating legislation concerning SMEs and giving recommendations on pieces of legislation that influence the business environment</li><li>• Proposing and compiling plans for better co-ordination and co-operation between the existing domestic and foreign organisations working for the development of SMEs</li><li>• Implementing programmes related to the creation and development of SMEs.</li></ul> <p>In 2008 the agency had 12 employees and a budget to allocate to different projects of approximately EUR 2.3 million. Although the agency does not include in this budget the donor's support, this is rather significant for Kosovo under UNSCR 1244/99. Meanwhile, a good lifelong entrepreneurial learning strategy provides a solid basis for the range of partners to move forward with lifelong entrepreneurial learning developments. This will require a more concerted commitment by the parties to enable further outcomes from the partnership arrangement already in place.</p>
<b>MK</b>	<p>Since the entry into force of the Law on One Stop-Shop System in 2006 and the maintenance of the trade register and the register of other legal entities, the former Yugoslav Republic of Macedonia has further improved the efficiency of its company registration system and reduced company registration fees. The Central Registry is currently able to process a company registration application in less than one day, down from five days in 2006 for a fee of approximately EUR 57. As typical of a one-stop shop system, the Central Registry issues the unique company registration number and obtains, on behalf of the new company the tax registration number, normally in a matter of a few hours. In order to further reduce start-up costs the former Yugoslav Republic of Macedonia has recently waived the minimum capital requirement for limited liability companies.</p>
<b>MNE</b>	<p>Montenegro has made particular strides to develop entrepreneurship education with an intensive piloting exercise within one municipality (Berane) in the country's least developed northern region. The strategic piloting effort follows the elaboration of a lifelong entrepreneurial learning strategy and action plan which captures the key lines of the Charter's indicators for entrepreneurship education and training. The challenge for the education and training authorities in co-operation with the world of enterprise is to move forward with the strategy and actions foreseen and to build on the policy learning and momentum developed through the 'Berane process'.</p>
<b>SRB</b>	<p>The Serbian government has made significant progress in taking action to promote competitiveness and support the technological capacity of SMEs. In January 2008 the government formally established the National Competitiveness Council. Its membership includes all key economic ministries, the Central Bank, the main private-sector associations, leading academics and business leaders. Its mandate is to conduct analysis on competitiveness issues, elaborate policy proposals, monitor policy development and foster programme co-operation it is expected to become a key policy forum.</p>

The result is a fragmented and often uncoordinated policy framework in which a relatively large number of projects and initiatives are launched. While these respond to local needs, they lack mechanisms for policy co-ordination, development of synergies among projects, and a productive exchange of experience among policy makers and stakeholders. The failure to fully implement company registration reform on a nationwide basis, and lack of common SME strategy and policy co-ordination institutions (already highlighted in the previous report) demonstrate how the situation has stalled. On the other hand, the country has made good progress on access to finance, an area less subject to policy fragmentation.

### **The impact of the global economic crisis on SME policy in the Western Balkans**

The assessment was completed just when the first indications of the impact of the growing global economic crisis on the Western Balkan economies were emerging. Over the last eight years, the Western Balkan economies recorded a long and sustained phase of economic expansion, with most of the economies recording gross domestic product (GDP) growth rates in excess of 5% over several years, increasing macro-economic stability, limited inflation and contained budget deficits (although growing current account deficits). The SME sector both contributed to and benefitted from sustained economic growth. The number of newly established SMEs increased significantly. Governments have been able to focus more on SME policy, as they have largely completed privatisation and the restructuring of the state-owned sector, and have channelled more resources to support SME policies.

Preliminary data for the last quarter of 2008 and the first quarter of 2009 show a sharp drop in external trade and industrial production, a contraction on foreign direct investment (FDI) inflows and a freeze on credit expansion accompanied by a significant slowdown in economic growth across the region. All this indicates that the global economic crisis is having an increasing impact on the Western Balkan economies. The key drivers that have underpinned growth in the region (domestic consumption, credit expansion and increasing capital inflows such as FDI and remittances) are losing strength and actions are needed to rebalance the large trade deficits that are common to all the Western Balkan economies.

The sudden and marked change in the macro-economic framework has significant implications for SME

policy: it heralds a review of policy priorities and an assessment of the policy tools available to respond effectively to the consequences of the crisis, and it may lead to a reduction of resources available to support SME policy.

Given that the crisis is not endogenous, but largely imported, and that the main transmission channels are trade, foreign direct investment and access to finance, it is likely that the crisis will affect segments of the SME population in different ways. At the time of writing these conclusions, data capturing the impact of the crisis on company behaviour and particularly on SMEs in the Western Balkan economies are not available. However it is possible to infer that the crisis will affect in the first instance companies that are more export-oriented, that have operations integrated into pan-European and international value chains (such as automotive and mechanical component producers) and that have made recent capital investments, either in expanding production facilities or in developing new products and markets. These companies are more vulnerable to the drop of external demand and to reductions in access to finance. Structural characteristics of Western Balkan companies may amplify the impact of the crisis. SMEs in the region tend to have a limited export market diversification, to rely largely on supplier credit for input financing, to depend largely on short-term revolving commercial bank credit (both for working capital and for investment) and to have limited access to equity financing.

While export, investment-oriented and innovative SMEs represent a small percentage of the total SME population, they contribute most to economic growth and employment generation, as highlighted in the section of this report dedicated to policies supporting high-growth SMEs (Part II). A sharp increase in business failures among those high-growth enterprises (due to external factors) may significantly reduce future economic growth.

On the other hand, the 2009 report shows that the relative weakness of SME policy in the Western Balkans lies specifically in the areas most relevant for high-growth enterprises, such as the provision of sophisticated business services, and the launching of programmes enhancing the technological capacity of SMEs. Governments also have limited experience in targeted SME policy, having given priority so far to horizontal measures.

## Future policy priorities

The crisis, therefore, implies a policy shift. It will be more feasible for governments that have already put in place schemes and facilities for targeted groups of enterprises. These include credit guarantee schemes, cost-sharing schemes, cost-recoverable schemes for innovation, and standard and business development activities, such those found in Croatia and Serbia and (to a lesser extent) Albania and the former Yugoslav Republic of Macedonia. Those schemes and facilities could be expanded and adapted to the needs arising from the crisis. They can be used as complementary support measures to resources channelled by the international financial institutions with the support of the European Commission, through the banking and financial sector.

For the remaining economies, the crisis should act as a stimulus to accelerate the pace of SME policy

development. For these economies an increase in donor support (both in terms of technical assistance transferring knowledge and the provision of advanced services to small enterprises) and financial assistance to expand pilot project schemes will be extremely important in this phase.

However, work should continue on the implementation of horizontal measures to improve the business and investment operational environment. While areas such as company registration are now less of a priority for most Western Balkan governments, regulatory reform, e-business and online services, building a regulatory and operational environment for the provision of financing schemes for SMEs (including equity funds and business angels) remain high priorities, as well as human capital development through entrepreneurship education and skill development.

## Key findings by policy dimension

**Table 2**

### Progress in scores per country (and Kosovo under UNSCR 1244/99) per dimension since the 2007 SME Policy Index Report\*

		ALB	BiH	HRV	XK	MK	MNE	SRB	REGION
Dimension 1: Entrepreneurship education and Training **	Change	N/A							
Dimension 2: Cheaper and faster start-ups	Change	+2.00	+0.50	+0.75	+0.25	+1.00	+0.25	+0.50	+0.75
Dimension 3: Better legislation and regulations	Change	+1.25	+0.25	+0.50	-0.25	+1.50	+1.00	+0.25	+0.75
Dimension 4: Availability of skills **	Change	N/A							
Dimension 5: Improving on-line access	Change	+1.50	0.00	+0.25	+0.75	+0.25	0.00	+1.00	+0.50
Dimension 6: Getting more out of the Single Market	Change	+0.75	0.00	0.00	+0.25	+0.50	-0.25	+1.25	+0.25
Dimension 7a: Taxation **	Change	N/A							
Dimension 7b: Access to Finance	Change	+0.75	+1.50	-0.25	+0.50	-0.25	+0.25	+0.75	+0.50
Dimension 8: Strengthening the Technol Capacity	Change	+0.00	+0.50	+0.25	+0.25	-0.25	0.00	+0.75	+0.25
Dimension 9: Successful E-Business Models	Change	+1.00	+0.25	+0.25	+0.75	+0.25	0.00	+1.00	+0.50
Dimension 10: Develop Stronger Representation	Change	+0.50	-0.50	+0.25	+0.25	-0.25	0.00	+1.50	+0.25

**Notes:** \*The progress in scores has been rounded up or down to the nearest 0.25.

\*\*For dimension 1, 4 and 7a comparison to the scores of 2007 has not been possible because the indicators within these dimensions have been significantly altered in the 2009 report

### **Dimension 1 - Entrepreneurship education and training**

The contribution of education to competitiveness is generating new policy interest in the potential of entrepreneurship education and training for improving productivity, innovation and economic growth. The Charter assessment focused particularly on policy in the area of entrepreneurship education and training as a driver for overall reforms. There have been clear movements by most countries to bring forward policy and strategy building in the area of entrepreneurship education and training. Several countries have already elaborated perspectives for lifelong entrepreneurial learning. However, there is a need for more systematic monitoring and evaluation of the range of activities in this area to ensure better efficiency of overall effort.

While non-formal entrepreneurship education and training (activities outside the school curriculum) is well developed, more efforts at building synergy with formal education could be considered in the bid to maximise the overall value of the various players contributing to the field. Although the Charter encourages more systematic co-operation among the players involved in entrepreneurship education and training, information and know-how exchange is generally confined to loose networks with little ambition amongst practitioners to make their achievements known. More developed networks could inspire confidence and trust amongst practitioners to publicise their work, allowing others to borrow on tried-and-tested ventures.

The assessment concludes with recommendations for more structured co-operation among education policy makers to step up lifelong entrepreneurship education and training. It also calls for more focused efforts to raise understanding of the entrepreneurship key competence amongst the education communities in terms of curriculum, teacher training, school governance and management.

### **Dimension 2 – Cheaper and faster start-up**

The 2009 report shows that there has been significant progress across the region in promoting faster and cheaper start-up. Progress has been more impressive in the registration phase. Today, new entrepreneurs can complete average registration procedures with company registers (specialised agency or commercial court) in less than five days from the time of application in all the Western Balkan countries, excluding Bosnia and Herzegovina. In most countries, it takes a day to obtain

the company registration certificate from the time of application, for a fee less than EUR 60. The pre-application steps have also been streamlined. Progress in the notification phase has been less marked. Two countries (Croatia, the former Yugoslav Republic of Macedonia) are moving towards the one-stop-shop model. Progress has been patchy and slow in the compliance phase, with intervention focusing on the elimination or reduction of minimum capital requirements for start-ups (the former Yugoslav Republic of Macedonia and Kosovo under UNSCR 1244/99). Over the last two years, Albania and Serbia were the most successful reformers in this dimension, while Bosnia and Herzegovina lagged further behind the regional average. Overall, the priorities set out in the 2007 report were only partially tackled and therefore remain largely valid for the near future. Governments need to find the right balance between the need to conduct checks and thorough inspections, and secure compliance with laws and regulations concerning health, security and environmental risks; and the desire not to put excessive burden on new business ventures. In the previous report, it was also suggested as a medium-term objective to transform the company registration body into a centre of collection and dissemination of company data for the public administration (tax administration, office of statistics and employment office) and the private sector, within the limits set by confidentiality rules and regulations. This would require the establishment of an electronic data bank covering the entire population of registered enterprises (not only the latest entries) and the integration of a number of new functions.

### **Dimension 3 - Better legislation and regulation**

Dimension 3 assesses three important elements for a stable and clear regulatory environment, namely regulatory reform, institutional framework and regulatory impact analysis. The countries' situation under this dimension has further improved over the previous report. The overall average for the Western Balkans has increased significantly. Currently all but two (Bosnia and Herzegovina and Kosovo under UNSCR 1244/99), are above level 3, considered a threshold at which a solid legal and/or institutional framework is in place. While the two least advanced economies still have to adopt their strategic framework and start implementing it, the other five economies should put further efforts in the implementation of the action plans of the strategies mentioned above.

In the field of 'Better regulatory environment' good progress has been registered in Albania, Croatia, the

former Yugoslav Republic of Macedonia, Montenegro and Serbia, both in terms of simplification of the existing legislation and gradual introduction of the regulatory impact analysis (RIA). As the process of reviewing the legislation has been completed in most of the countries, further effort should be putted in eliminating the redundant legislation and the systematic use of RIA.

#### **Dimension 4 - Availability of skills**

With increased recognition being afforded to human capital in the wider bid for more competitive enterprises, the Charter assessment considered training availability, with particular emphasis on training for new ventures and expanding businesses. Overall, there is a lack of comprehensive data on enterprise training, including training for start-ups and growing enterprises. What data are available are invariably spread across different organisations and serving different purposes, making the task of quantitative assessment difficult. Nonetheless, there is evidence of a growing recognition of the importance of reliable data for more targeted developments in enterprise-based human capital. A regional proposal for countries (including Turkey) to gather information on enterprise skills provides an opportunity for the region to overcome the constraints of weak data.

Data aside, the assessment identified considerable effort to promote training in all countries through good networks of training providers (for the most part public training services), although the extent to which this training is directly accessible by enterprises is not clear. Similarly, information on private training providers is generally not readily available, suggesting an under-developed training market. The assessment points to the need for more developments in the area of quality assurance in training; this will generate confidence in, and demand for, training by enterprises.

The assessment concludes with recommendations for more systemic developments in enterprise training intelligence as well as measures to promote a more developed training market.

#### **Dimension 5 - Improving online access**

E-government services for SMEs have emerged in the Western Balkans, but only Croatia holds a clear e-government strategy. Albania, Montenegro and Serbia have made great strides in rendering government services more accessible online (including the provision of relevant online business information and the introduction of

online services for filing tax returns or social security). The key weakness within this dimension remains the lack of SME-dedicated online portals, which would make searching for information less cumbersome by bundling SME-relevant information and links (that are regularly updated), and allowing for interaction between SMEs and the administration.

#### **Dimension 6 – Getting more out of the Single Market**

Progress on the two indicators related to export promotion and enhancing SME competitiveness has been limited across the region. Only Albania and Serbia have recorded significant improvement in their performance on both indicators and only three countries (Albania, Croatia and Serbia) have a structured export support scheme, covering export promotion, export insurance and export financing.

The global economic crisis is having a significant impact, especially on companies that rely on exports to the EU market and on those that operate in network industries (such as the automotive, electronic and mechanical sectors) and supply components to manufacturers based in EU countries. SMEs in the Western Balkans have to deal with a drop in the external demand, a shortage of supplier and buyer credit, and sudden shifts in their competitive position due to the sharp currency movement across East and South East Europe. In this situation, governments in the Western Balkans have to address simultaneously contingent and structural issues. On export support, the priority in this phase is to provide export insurance and export credit to companies affected by the increase in commercial risk in export market and the drying up of liquidity. On export promotion, priority should be given to market diversification, for instance, pursuing market opportunities arising from the implementation of the 2006 Central European Free Trade Agreement. On enhancing competitiveness, countries that have already launched support programmes (such as Albania, Croatia, the former Yugoslav Republic of Macedonia and Serbia) should closely monitor the impact of those programmes and adapt the range of supporting tools to the differentiated needs of SMEs. Given the significant contribution of donor-funded programmes in these areas, all the Western Balkan countries need donor-supported programmes that are integrated and co-ordinated into a government medium-term strategy for competitiveness and support to high-growth enterprises. It is also essential that lessons learned across various business support programmes are reviewed and compared, then integrated into the government action.

## Dimension 7a – Taxation

The assessment in this dimension aims to score seven countries in the Western Balkans on the basis of rough measures of progress to date in implementing various frameworks and in exploring a number of aspects of the tax treatment of small businesses, given policy interest in assessments of the tax burden on small businesses and in understanding possible tax effects on the cost of funds, tax arbitrage behaviour and risk-taking, and tax compliance costs. While all countries forecast main tax revenues, and can generate rough estimates of effects of broad-based tax changes on aggregate revenues, no economy in the Western Balkan region has yet implemented micro-simulation models capable of estimating disaggregate revenue effects, and simulating the tax revenue consequences of detailed fine-tuning of their tax systems. However, the Federation of Bosnia and Herzegovina, the Republika Srpska<sup>1</sup>, the former Yugoslav Republic of Macedonia and Montenegro are taking steps to implement such models. Croatia and the former Yugoslav Republic of Macedonia recently participated in an OECD tax modelling workshop, aimed at assisting countries in pursuing micro-simulation frameworks. Limited analysis has been undertaken of effects on the cost of capital of small business of double taxation of profits of incorporated firms through the region, although in Kosovo under UNSCR 1244/99 and Montenegro studies have been undertaken to examine potential effects of double taxation on equity financing, and alternative integration systems have been examined. Throughout the Western Balkans, no economy has yet to systematically carry out studies of tax arbitrage by small business owners. A review of income tax rates on self-employed business income, dividends, interest and capital gains suggests that care has been taken in many economies to limit tax planning opportunities of owner/workers of closely held companies. Yet significant rate differences are observed in some cases, in particular when account is taken of social security contributions levied on wage income. Additional analysis and sharing of experience across the region would be welcome. In Albania, the Federation of Bosnia and Herzegovina, the Republika Srpska, Croatia and the former Yugoslav Republic of Macedonia, detailed analyses have not yet been carried out to assess implications of alternative loss treatment on investment in small firms with relatively high-risk business ventures, and on scope for tax-avoidance. Montenegro has analysed the potential for its business loss-offset provisions to influence risky investment in small businesses. Kosovo under UNSCR 1244/99 has also recently assessed its business loss-offset rules. Finally, a number of Western Balkan countries (Albania, Croatia, the Federation of Bosnia and Herzegovina, the Republika Srpska) as well Kosovo under

UNSCR 1244/99, have made significant strides in addressing tax compliance costs, arguably the most important impediment to address.

## Dimension 7b – Access to finance

The Access to finance dimension of Dimension 7 is made up of 2 subdimensions: credit environment and financial products for SMEs. Across the region, there has been substantial progress in improving the credit environment. Two news indicators have been included in the SME Policy Index 2009 assessment for this subdimension: registration systems for movable assets and credit information services are in place in most of the countries (with exception of Kosovo under UNSCR 1244/99 for both indicators and the former Yugoslav Republic of Macedonia for credit information services). The Asset-backed bank lending is the main source of external financing for enterprises. Since the last assessment, asset-backed bank lending has increased in importance while the reliance on internal funds and retained earnings has decreased. All countries have established credit guarantee schemes. However, until assessment cut-off date, only the former Yugoslav Republic of Macedonia followed EBRD's previous recommendation that credit guarantee scheme be privately managed in order to achieve the most efficient allocation of resources. Credit information services are in place in all countries, however, not yet fully developed. Collateral requirements remain very high in most of the countries with the exception of Albania and Bosnia and Herzegovina. The global financial downturn furthermore encourages banks' conservative lending policies. Access to (and reliability of) information from cadastres is still limited and has not improved since last assessment. Microfinance facilities are also well developed in a most countries, with the presence of international microfinance institutions. Access to capital markets for SMEs is still problematic and the availability of risk capital is very limited. The venture capital industry is developing, although for the moment the only exit possibility is direct sale. The leasing industry is already an important channel of finance for the SME sector. Relevant legislation is in place everywhere except for Kosovo under UNSCR 1244/99 and leasing companies are operating. Finally laws and procedures on distressed companies, receivership and bankruptcy are formally in place, but legislation is at an early stage of implementation for Albania, Croatia and the former Yugoslav Republic of Macedonia. All countries are well developed in terms of access to financial products for SMEs (here specifically assessed: the leasing industry and venture capital funds), but there is still scope for improvements. Most of the mechanisms conducive to a good credit environment are

formally in place (with the exception of Kosovo under UNSCR 1244/99), but the level of implementation varies across the indicators and countries. There is a need to increase efforts throughout all categories and countries and to sustain efforts where significant progress has been made (credit guarantee schemes in the former Yugoslav Republic of Macedonia, collateral requirements in Bosnia, leasing industry in Serbia).

### **Dimension 8 – Strengthening the technological capacity of small enterprises**

All across the region, government policies directed at strengthening the technological capacities of SMEs are at an early stage of development. Croatia is the most advanced in the three areas of technology dissemination, technology co-operation, and research and development of inter-firm clusters. It has launched a comprehensive technological development programme (BICRO). In a number of other countries (Bosnia and Herzegovina, the former Yugoslav Republic of Macedonia and Serbia), technology support programmes are mostly still in a pilot phase, although progress has been recorded in Bosnia and Herzegovina, and Serbia in the cluster development area. Albania, Kosovo under UNSCR1244/99 and Montenegro are at a very early stage of policy elaboration. There have been positive developments in the intellectual property rights (IPR) area (in terms of institutional development and legislative upgrading and, to a lesser extent, policy enforcement) with a number of countries: Croatia, the former Yugoslav Republic of Macedonia and Serbia. As a way forward, government should further extend the support to initiatives establishing inter-firm clusters and networks, integrating those initiatives with other enterprise-supporting schemes (voucher schemes, business incubators, innovation supporting schemes, etc.). Governments should also continue to change the orientation of the existing clusters from the traditional sectors to higher value added ones. As argued in the section on high-growth enterprises, in order to forge an environment that encourages innovation and growth, it is important to move forward on diverse yet complementary areas (intellectual property rights, business incubators, cluster development and skills development). As noted in the previous report, it is vital to ensure a high level of co-ordination among the Ministry of Economy, Ministry of Education and Science, the private sector, universities and research institutes. Finally governments need to continue to act on IPRs; they need to devote more resources to the enforcement of IPR legislation through communication campaigns, training of officials and monitoring of IPR cases to ensure results, particularly in economies with weak IPR enforcement records.

### **Dimension 9 - Successful e-business models and top-class business support**

Although the range and quality of business services have generally improved over the last two years (due in part to the arrival of renown international business service providers), there is still a strong need for greater clarity, quality service standards and better co-ordination of business support strategies. Most business incubators, for example, are still the product of *ad hoc* initiatives that disappear once the funding does. There is thus a continuing need in the Western Balkans to establish national strategies for the development of business incubators, linking these with measures to encourage innovation and ensuring that clear funding and performance measures are in place. Furthermore, there is an urgent need in most Western Balkan countries and Kosovo under UNSCR 1244/99 to complete the regulatory framework for introducing the electronic signature and to establish a functional and legitimate accreditation body. This is a precondition to developing electronic commerce and more advanced online business-to-business functions, as well as for making the most of online government services.

### **Dimension 10 - Developing stronger and more effective representation of small enterprises' interests**

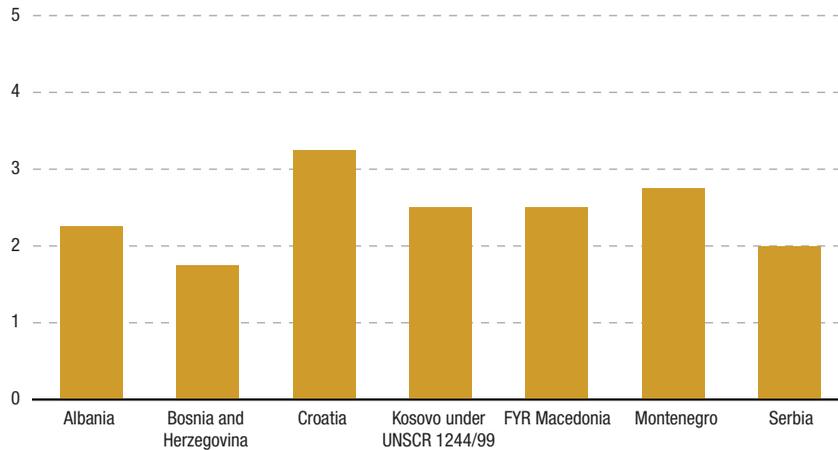
Dimension 10 deals with the effectiveness of SME representation and the involvement of the public administration and the business community in public-private dialogue. The overall situation improved in most of the economies in the region since the 2007 report due mainly to two aspects: the reforms of the chambers of commerce and improved framework for public-private dialogue.

Both the public administration and the private sector need to step up the scope of public-private dialogue and its quality. The main challenge for the government is to consult the business community systematically and early in the process, while the business community must build up the necessary capacity to conduct consultations within the different business associations and to provide well documented proposals and comments. Although there are numerous business associations and a system of chambers of commerce in each economy, this capacity is still relatively limited. Regarding the format of public-private dialogue, despite the fact that only Bosnia and Herzegovina is missing a body for this purpose at national level, all the others have to improve their own system in order to hold regular meetings and to improve the transparency of the system.

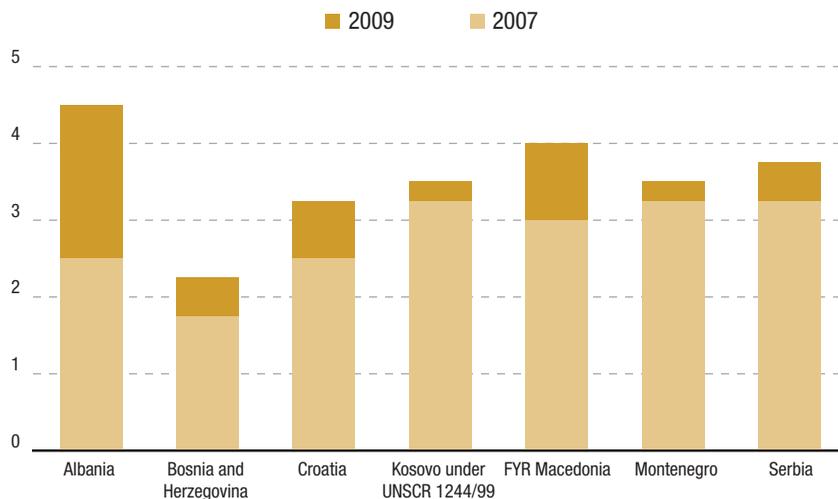
## Progress across the Charter dimensions: Overall SME Policy Index scores<sup>2</sup>

The following figures show the SME Policy Index scores for each economy and Charter dimension, comparing the current results to those published in the SME Policy Index 2007 Report. Due to the large number of new indicators, the results in dimensions 1, 4 and 7a are not comparable to the results from 2007.

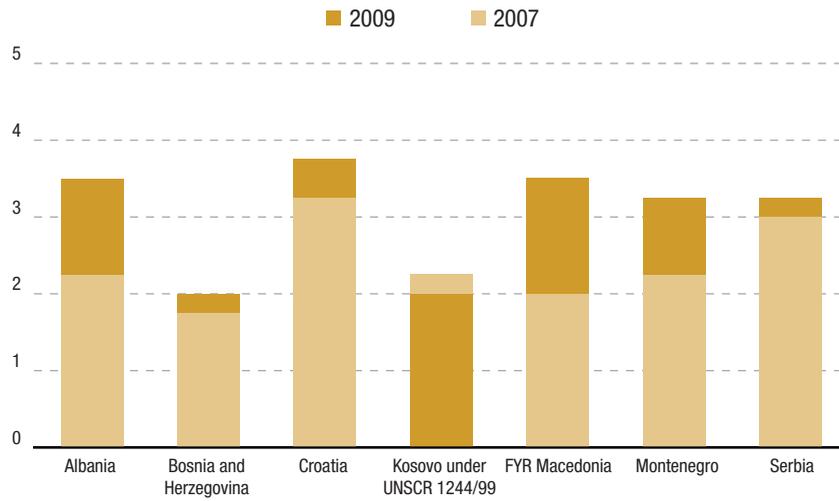
### Dimension 1: Entrepreneurship education and training



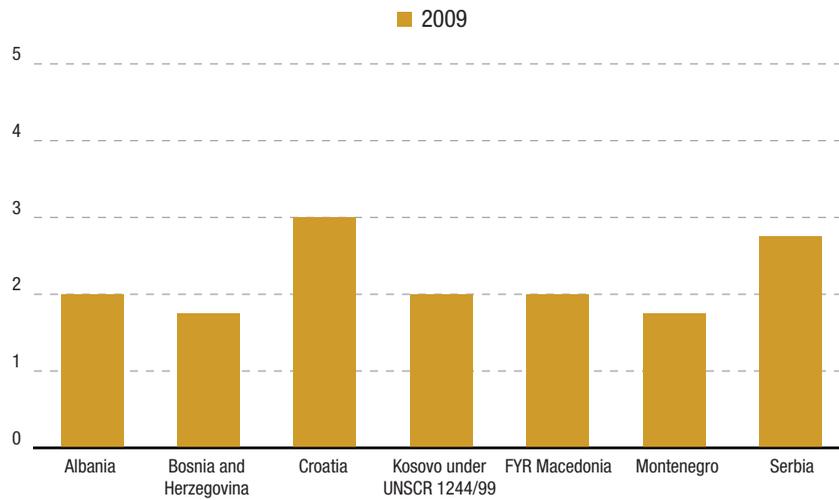
### Dimension 2: Cheaper and faster start-up



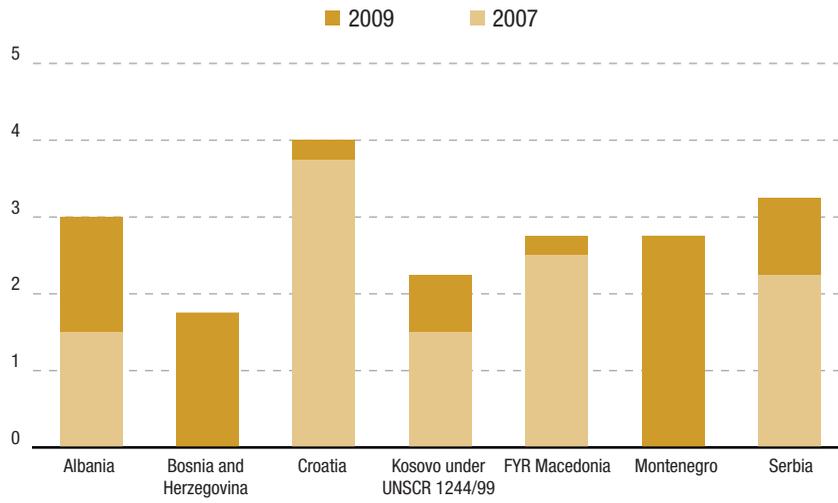
### Dimension 3: Better legislation and regulation



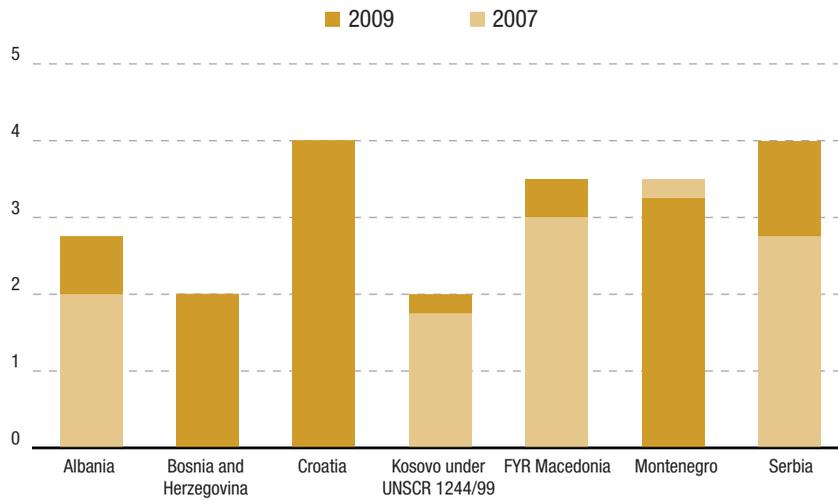
### Dimension 4: Availability of skills



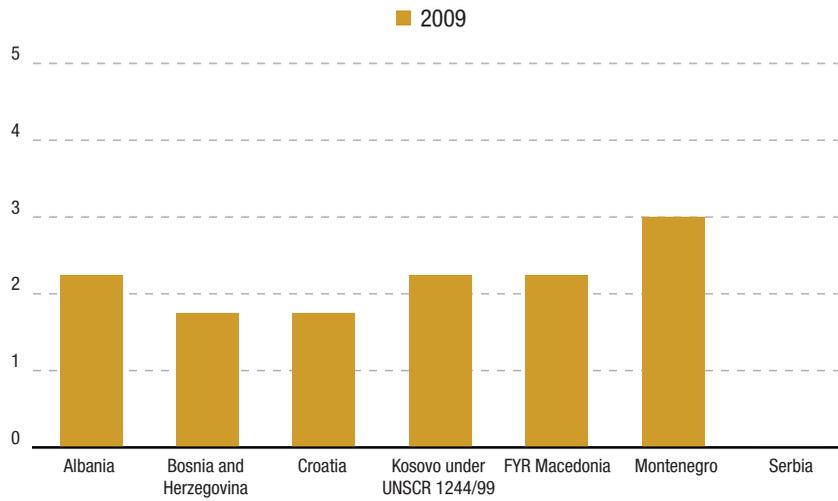
### Dimension 5: Improving online access



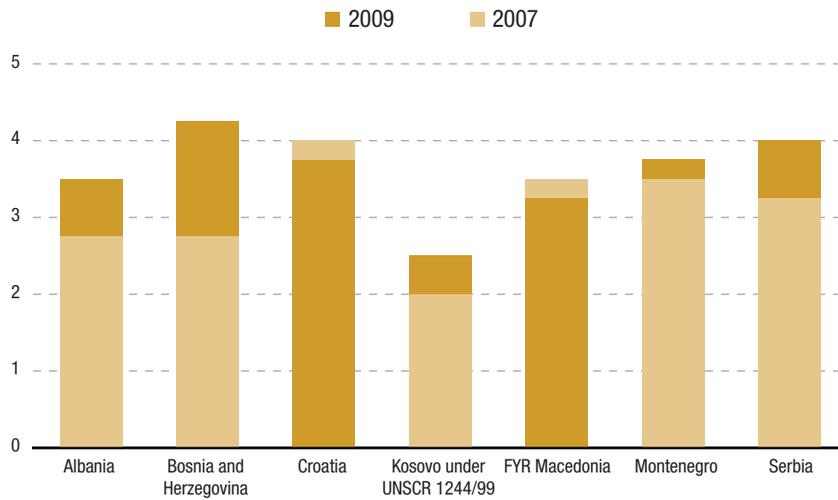
### Dimension 6: Getting more out of the Single Market



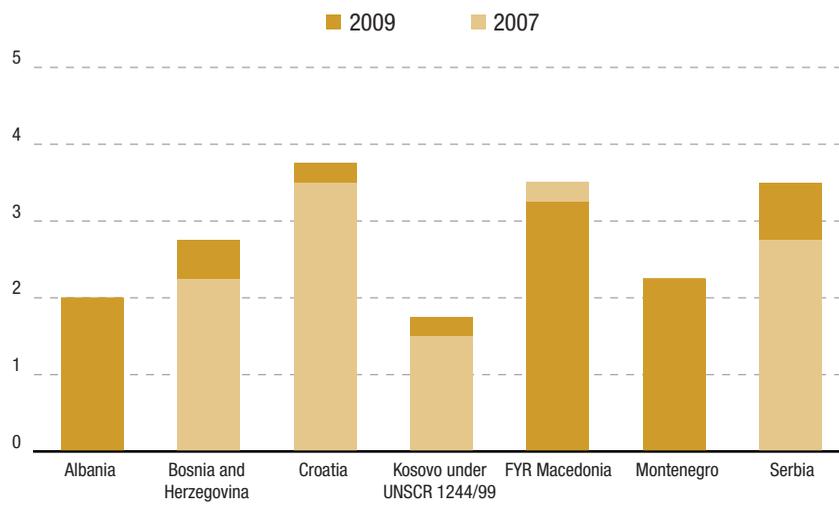
### Dimension 7a: Taxation<sup>3</sup>



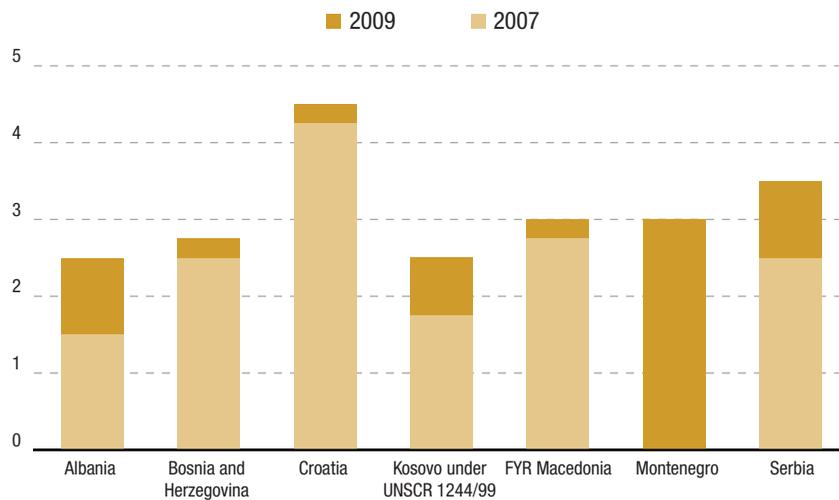
### Dimension 7b: Access to finance



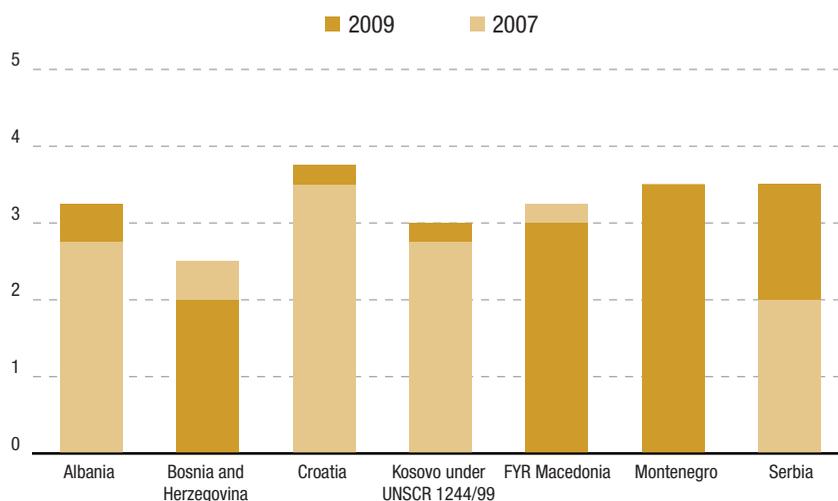
## Dimension 8: Strengthening the technological capacity



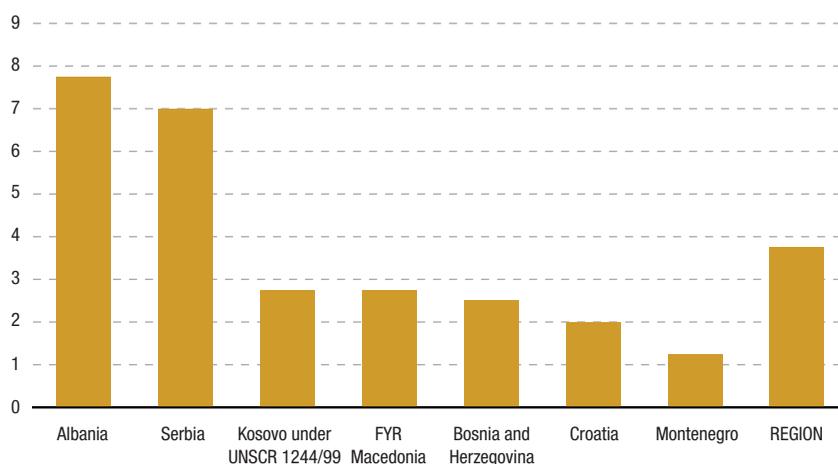
## Dimension 9: Successful e-business models



## Dimension 10: Develop stronger representation



## Overall cumulative changes in scores since 2007 SME Policy Index in the Western Balkans



## Notes

1. Within this assessment, the Republika Srpska and the Federation of Bosnia and Herzegovina were assessed separately due to the differing tax systems. The Brcko District was not assessed.
2. Although this report is published in 2009, its data collection took place in 2008. For the SME Policy Index Report 2007, data were collected in 2006. All SME Policy Index scores have been rounded up or down to the nearest 0.25
3. The assessment for dimension 7a: taxation was not completed for Serbia due to a lack of data.

