



**ENTERPRISE POLICY  
PERFORMANCE  
ASSESSMENT**

**REPUBLIC OF SERBIA**

**SERBIA AND MONTENEGRO**

**JANUARY 2005**



**STABILITY PACT**  
FOR SOUTH EASTERN EUROPE



**INVESTMENT COMPACT**  
FOR SOUTH EAST EUROPE



**European Bank**  
for Reconstruction and Development





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**The Stability Pact for South Eastern Europe** is a political declaration and framework agreement adopted in June 1999 to encourage and strengthen co-operation among the countries of South East Europe (SEE) and to facilitate, co-ordinate and streamline efforts to ensure stability and economic growth in the region. (see [www.stabilitypact.org](http://www.stabilitypact.org))

**The South East Europe Compact for Reform, Investment, Integrity and Growth ("The Investment Compact")** is a key component of the Stability Pact under Working Table II on Economic Reconstruction, Development and Co-operation. Private investment is essential to facilitate the transition to market economy structures and to underpin social and economic development. The Investment Compact promotes and supports policy reforms that aim to improve the investment climate in South East Europe and thereby encourage investment and the development of a strong private sector. The main objectives of the Investment Compact are to:

- Improve the climate for business and investment.
- Attract and encourage private investment.
- Ensure private sector involvement in the reform process.
- Instigate and monitor the implementation of reform.

The participating SEE countries in the Investment Compact are: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, the Former Yugoslav Republic of Macedonia, Moldova, Romania, Serbia and Montenegro. Building on the core principle of the Investment Compact that "ownership" of reform rests within the region itself, the Investment Compact seeks to share the long experience of OECD countries. It provides region-wide peer review and capacity building through dialogue on successful policy development and ensures identification of practical steps to implement reform and transition.

The work of the Investment Compact is actively supported and financed by seventeen OECD member countries: Austria, Flanders (Belgium), Czech Republic, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Norway, Sweden, Switzerland, Turkey, United Kingdom and United States. (see [www.investmentcompact.org](http://www.investmentcompact.org)). The European Commission (EC) has, through DG Enterprise, contributed to the funding for this report. The Investment Compact herewith acknowledges this assistance.

The Enterprise Policy Performance Assessments (EPPAS) are an output of the eSEE Enterprise Forum, a regional policy initiative sponsored by the Investment Compact for South East Europe. The EPPA reports have been jointly produced by the OECD and European Bank for Reconstruction and Development (EBRD), in consultation with the European Commission (DG Enterprise and Industry). The EPPA reports have been initiated by Declan Murphy, Programme Director of the Investment Compact, and their preparation has been co-ordinated by Antonio Fanelli (Principal Administrator, OECD), Francesca Pissarides (Senior Economist, EBRD) and Peter Sanfey (EBRD).

Background research and support was provided by G17 Institute, Serbia and Montenegro, which provided the first draft. The research team consisted of: Mirosinka Dinkic (Project Leader and author); Kosovka Ognjenovic, Goran Petkovic, Ivana Petrovic (authors); Marija Vukotic, Iva Jovanovic, Ruzica Savcic (project collaborators) and Ivana Radovic (translator). The report has benefited significantly from input and comments from Declan Murphy, Programme Director of the Investment Compact (OECD) and Antonio Fanelli, Principal Administrator (Investment Compact, OECD), and the assistance of Georgiana Pop (OECD) and Susan Hodgson (OECD). Jim Bourke (OECD consultant) has provided expert guidance on the report.

The assessments and views expressed in this report are those of the Investment Compact Team of the OECD secretariat and the EBRD Office of the Chief Economist and do not necessarily reflect the views of the institutions participating in this enterprise policy performance assessment of the OECD and EBRD member countries.

## FOREWORD

In all countries the government and its agencies have a fundamental lead role to play in providing an environment favourable to business operations and conducive to private investment. This is especially true for small business. Small and medium-sized enterprises are the backbone of most economies today. In order to flourish and grow they need an environment that facilitates and enables business start-up, does not hamper them with excessive and costly regulations and facilitates access to finance and business services. In this respect there is an urgent need in South East Europe (SEE) to design and implement an effective enterprise policy, as the level of private investment still lags behind that of advanced countries.

For these reasons, in 2002 the OECD and the EBRD launched the Enterprise Policy Performance Assessments (EPPAs) in the framework of the Investment Compact for SEE Programme. The EPPAs consist of a series of reports covering all the countries of South East Europe, assessing the quality of the government policy for the SME sector and regularly monitoring its implementation. In 2002 the Investment Compact published nine country reports (separate reports were produced for Serbia and Montenegro, respectively) as well as a Regional EPPA report measuring progress on SME policy implementation in the SEE against a set of good practices and benchmarks.

As part of the 2004 EPPA programme the Investment Compact presents the 2004 edition of the Enterprise Policy Performance Assessment for Serbia. The format of the report is the same as last year, allowing for a direct comparison of the progress achieved since the 2003 EPPA.

The 2004 report has been prepared by the OECD and the EBRD in close consultation with the European Commission, which also provided financial support to the programme. Excellent synergies have been developed between the EPPA and the European Union Charter for Small Business, with the EPPA providing a set of policy recommendations and priority actions to the government and small business community in those policy dimensions covered by the EU Charter. In order to improve the link between the EPPA and the EU Charter, the scope of the 2004 EPPA has been expanded. The EPPA reports now cover seven policy areas, adding entrepreneurship, vocational training and access to technology to the previous set of six policy dimensions (institutional framework, regulatory environment, tax policy, access to finance, advisory services, business incubators), bringing their scope closer to that of the EU Charter.

This Enterprise Policy Performance Assessment report is presented as an independent and constructive contribution to the debate on enterprise policy in Serbia, with the principal aim of facilitating the reform implementation. The OECD, EBRD and European Commission will monitor progress and seek to provide active support on implementation in partnership with the SEE countries in 2005.



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## INTRODUCTION

### Scope and Structure of the Enterprise Policy Performance Assessments (EPPAs)

The 2004 EPPA Country Reports have been prepared jointly by the OECD and the EBRD, in consultation with the EC and with the assistance of a network of South East European and international consultants.

In 2002 the OECD Investment Compact and the EBRD launched the Enterprise Policy Performance Assessments (EPPAs) with the aim of producing independent and comprehensive assessments on an annual basis of the enterprise policy carried out by the government institutions in the each of the countries of South East Europe.

The country assessment is the result of the elaboration of a number of inputs: insights from entrepreneurs and SME owners, collected through focus group discussions and interviews, contributions from SME experts, policy makers, representatives of the association of private enterprises, international and bilateral organisations dealing with SME issues, desk research and analysis, combined with the experience and judgement of OECD and EBRD experts. The assessment was originally designed to address six policy dimensions, at the core of enterprise policy.

Nine EPPA reports, one for each of the SEE country, with Serbia and Montenegro being assessed separately, and a Regional SEE Assessment Report were published by the Investment Compact in 2003 and disseminated throughout the SEE Region. All the reports are available from the Investment Compact web-site: [www.investmentcompact.org](http://www.investmentcompact.org).

The EC General Directorate for Enterprise and Industry joined the OECD-EBRD team in October 2003 with the aim of developing synergies between the EPPAs and monitoring of the implementation of the best practices contained in the European Charter for Small Enterprises, signed by all the SEE countries.

The 2004 EPPA Country Reports represent both a continuation and an expansion of the work started in 2002. The scope of the reports have been expanded in 2004 to include a seventh policy dimension covering entrepreneurship, vocational education and access to technologies, thereby better integrating the scope of the EPPAs with that of the European Charter on Small Enterprises.

The 2004 framework of research for analysis of the performance of enterprises policy thus consists of the following dimensions of small enterprise policy:

- Institutional framework for SMEs policy.
- Rule of law and regulatory framework.
- Tax policy for small business.
- Financial instruments for new and small companies.
- Business consulting services for new and small enterprises.
- Business Incubators.
- Entrepreneurship, vocational education and access to technologies.



The 2004 EPPA Country Reports are structured in two parts. Part I includes an overall assessment of enterprise policy, looking at progress made since the publication of the 2003 EPPA report. It also contains an updated list of policy recommendations and a set of priorities for short term action.

Part II consists of two chapters. The first contains the insights of entrepreneurs and SME owners and managers, while the second chapter is dedicated to analysis and assessment, including a report on the implementation of the policy recommendations listed in the 2003 EPPA Country Report.

## **The EPPA Methodology**

The EPPA methodology has been designed to provide insights and assessments of the performance in the *implementation of policies* to improve the investment environment for small business. The EPPAs have been conducted on a standard basis in all countries of the region and provide a benchmark for (a) highlighting key reform issues (b) measuring private sector insights and assessments of the business environment (c) assessing progress on a country-by-country basis and (d) comparative cross-country review for the SEE region.

The policy assessments have been formulated on the basis of the following inputs:

### **Focus group research:**

Focus group discussions were held with SME representatives. The focus group discussions were guided by a question template, applied to all the SEE countries, derived from extensive case study work on good practice in transition economies, including South East Europe, and OECD country experience (OECD-UNIDO, 1999).

### **Individual SME interviews and expert interviews:**

Individual SME interviews were used to cross check the focus group research and to provide further insights on key issues in each of the SEE countries.

Expert interviews were conducted to cross reference information from the focus groups and individual SME interviews and to contribute to overall views.

### **Desk research:**

Examination of existing reports, databases, documents, etc. was conducted by country-based experts/consultants, selected for their enterprise policy knowledge and experience, under the supervision of the OECD Investment Compact team.

### **Expertise from the OECD, the EBRD and the EC:**

A team of experts from the OECD, EBRD and from OECD countries has reviewed inputs from focus groups, interviews and desk research and elaborated the country assessments.

A detailed description of methodology used in the research is presented in Annex 3.



## Part I

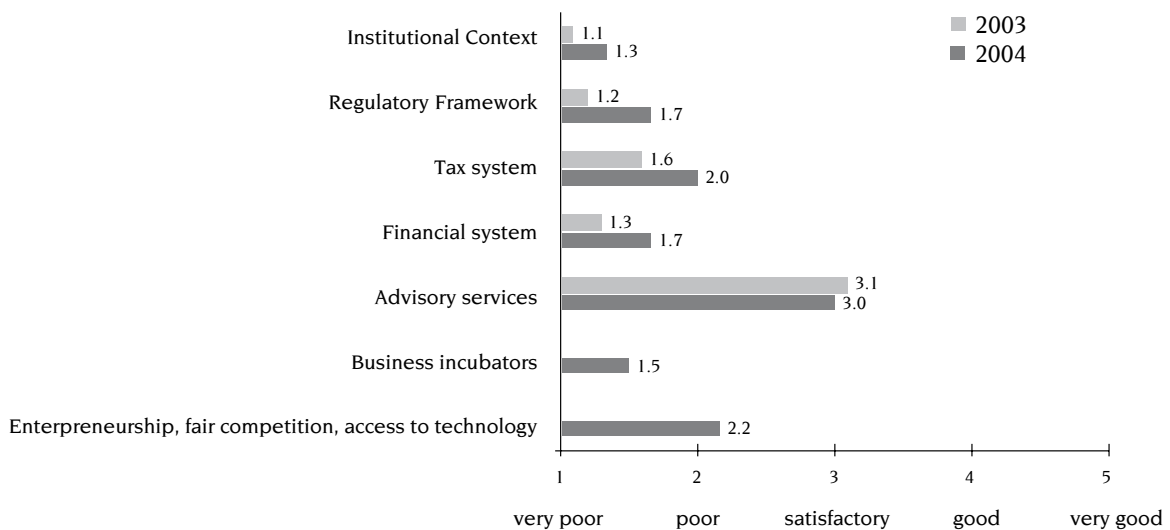
# OVERALL ASSESSMENT AND POLICY RECOMMENDATIONS

### Overall Assessment

The EPPA 2004 indicates that, since the completion of the previous EPPA report in March 2003, Serbia has made progress in implementing better policies for the SME sector. The overall picture is that of a gradual, but limited and uneven progress over the broad spectrum of the seven policy dimensions covered by the EPPA report.

From a total of 42 policy recommendations listed in the 2003 EPPA report, covering six policy dimensions, there has been significant progress in the implementation of 3 of them, limited progress for 24 and no relevant progress for the remaining 15 recommendations, as reported in Chapter 2.

**Figure 1.1. Average Ratings by SME Owners and Managers of the Seven Dimensions of Good Practice, 2003 and 2004**



The views of the SME owners and managers in Serbia who participated in the focus groups in 2004, confirm a picture of steady, but patchy progress. With the exception of advisory services, the 2004 ratings for all policy dimensions, were marginally better than those of 2003. In absolute terms, except for advisory services, the policy performance ratings remain very low, within or just above the ranking of “poor”, confirming the general dissatisfaction of entrepreneurs with the current operational environment and the slow pace of reform.

The low rating level also provides an indication of how much more remains to be done in terms of policy implementation and communication with the business sector. However, SME owners and managers perceived an improvement in the public image of entrepreneurs, in the quality of professional education and in access to technology. In brief the assessment shows:

## **Institutional Framework for SME Policy**

Looking at the individual policy dimensions, the assessment is that the institutional framework for SME development has been developed and strengthened, but further work is still needed. The framework for policy elaboration and implementation is clear and well defined, with the Ministry of Economy acting as the policy making body and the SME Agency (ASME) as the executive agency in charge of the SME strategy implementation. ASME, in a relatively short time has reached a good overall operational level and is engaged in the implementation of the SME development strategy for the 2003-2008 period. It launched a number of programmes during its first year, developed an extensive communication campaign and built a network of 14 regional development agencies and centres. However, the level of resources allocated to it remains a major issue. ASME's annual budget is one of the lowest in SEE and is not commensurate with the ambitious targets set for the 2003-2008 strategy for SMEs and Entrepreneurship Development. Inter-ministerial co-ordination, private sector consultation and donor co-ordination also needs to be further developed.

## **Rule of Law and Regulatory Environment**

In terms of the development of the rule of law and the regulatory environment for SMEs, there has been some notable progress in 2004, after a phase of inaction due to several rounds of presidential elections and then the general elections. A number of laws with important implications for the enterprise sector have recently been passed, others have been amended or improved.

The most significant legislative progress has been in the area of business registration, with the approval in May 2004 of a new set of laws designed to radically simplify registration procedures, cutting time and costs. The new legislation will introduce a registration system in Serbia, designed to the highest international standards. The challenge is now to ensure full follow-up and effective implementation and operation.

The legislative upgrading and the reform of the regulatory framework, however, is still far from being complete. The new Company Law, for instance, is still awaiting final approval. The government is making considerable efforts to accelerate the pace of legislative reform, after the delays accumulated during the long electoral phase. The general perception of entrepreneurs is that legal and regulatory reforms are taking place too slowly and sometimes SMEs are not made aware of the benefits likely to be generated from the changes, as was the case for instance with the Law on Planning and Construction, approved last year.

In other cases the changes are not clearly enough defined, causing problems in implementation. Entrepreneurs still strongly complain that regulations are not applied equally to all economic entities. Some enterprises, in particular the larger state-owned enterprises, are allowed to avoid compliance with tax, social security contributions and environmental regulations. Non-compliance in this case operates as a kind of disguised subsidy for state-owned enterprises, allowing them to compete unfairly with private companies. Complex regulatory procedures can still sometimes only be completed either with help of contacts or acquaintances within the system or with the help of money.

## **Tax Policy for Small Business**

There has been significant improvement in the tax regime since 2003, both in terms of a net reduction in the tax burden on enterprises and in terms of increased transparency and the balance of the tax system. With a rate of 10%, Serbia has one of the lowest Corporate Income Tax rates in the region and among all the transition countries. The tax burden can be further reduced by availing of a range of tax credits and allowances linked to investment and employment generation. There are great expectations among SMEs that the introduction of VAT, scheduled for the 1<sup>st</sup> of January 2005, could have a critical impact in creating a level playing field and in reducing unfair competition from tax evading companies.

## Financial Instruments for New and Small Business

The banking sector in Serbia is now more stable, after the first phase of banking sector restructuring. There are 46 banks currently operating in Serbia (not including Kosovo and Metohija). This may be too many for a market of 7.5 million inhabitants and with a GDP of only CSD 1,100 billion (USD 2,500 per capita in 2003), but increased competition among commercial banks, for the moment still limited, should contribute to improving services and lending conditions. The range of services available to corporate clients is still limited. There are indications that the banks have started to pay greater attention to private clients but are perceived to be overly cautious in granting loans to SMEs, fearing non-performance. The micro-finance sector is growing, with an excellent repayment record, a clear indication that there is a market for small commercial loans. What is required is a more pro-active and innovative approach by the banking sector.

The priority now, from the enterprise development perspective, is to pass the set of legislative measures, new laws and amendments that underpin the development of the financial sector and that will help to provide better access to financing for SMEs, such as the Law on Enforcement Procedures, the Law on Contracts, the Law on Pledge of Movable Assets, *etc.*

The government should continue to promote the restructuring of the banking sector, opening the sector to healthy competition, and at the same time should complete the legal framework needed to develop banking operations. The two paths should develop in parallel to produce over the medium term the maximum of benefits to the private enterprise sector.

## Advisory Services

Entrepreneurs gave advisory services the best rating among all the policy dimensions. They are fairly satisfied with the quality of service of private consultants, although some of them have raised concerns about the professionalism of some advisory services, and are less satisfied with the services provided by publicly supported business centres. This is a common feature across all the SEE countries. Government should look closely at how to bring the network of the Chamber of Commerce closer to the needs of the small business sector and how to use the business associations as a channel to deliver basic information and services to SMEs. The introduction of a certification system for independent business consultants would help to address the issue of quality and professionalism.

## Business Incubators

Business incubators have good potential, given the growth of, for example, an emerging ICT and technology sector in Serbia. The development of a Serbian Business Incubator programme, at the moment still at a very initial phase with just one business incubator in operation and pilot project, supported by Norway, under development, should be pursued and links should be established with universities and research centres. Entrepreneurs are particularly interested in programmes linking business incubators with the financial and legal benefits to start ups.

## Entrepreneurship, Vocational Education and Access to Technology

More promotion and awareness of the concept of entrepreneurship is needed. The consensus is that the vocational education system in Serbia is too focused on theoretical knowledge and pupils are leaving school without adequate practical knowledge. Many SMEs are not aware of the training programmes designed for entrepreneurs. The available training programmes are often not “tailor-made” for local entrepreneurs and they do not address the specific problems that entrepreneurs are encountering in their day-to-day work. Existing SMEs need stronger management and technical training support programmes.

### Box 1: Serbia and the EU Charter for Small Enterprises

Serbia and Montenegro signed the European Charter for Small Enterprises in June 2003. The Charter, a Pan European initiative endorsed by all the EU members states, the EU candidate countries, the countries of the Western Balkans, outlines ten policy areas which are instrumental to improving the business environment for small companies. These include regulatory reform, access to finance, business advocacy, entrepreneurship education, competitiveness, etc. and broadly cover the same policy spectrum as the EPPAs. Under the framework of the EU Charter Process, in 2003 the Serbian government identified a set of targets related to initiatives designed to help small businesses.

Progress on target implementation is reviewed annually in a report prepared by the Serbian government and published by the European Commission, together with the other countries in the Western Balkans. The second annual EU Charter Report for the Western Balkan Region, containing the country reports and a regional overview prepared by the European Commission, is scheduled to be published in January 2005.

The EPPA report intends to contribute to the EU Charter process, with an independent and business oriented policy implementation assessment. The list of the EU Charter targets for the policy dimensions covered by the EPPA, together with comments on the target implementation status is reported in Annex 4.

Overall, the targets set by Serbia in 2003 appeared to be relevant for the small business sector and broadly in line with the EPPA 2003 policy recommendations. As the 2004 EPPA shows, good progress has been made in the area of company registration, entrepreneurship training and consultancy services for small business, where an innovative voucher system has been introduced with technical assistance from the EC.

### Priority Reform Issues for Action

1. The Ministry of Economy (MoE) should set a number of clearly defined and realistic milestones (as well as intermediary objectives) related to the implementation of the National SME Strategy and structure and equip ASME on the basis of the resources needed to reach those milestones.
2. Fully implement the new Law on Registration of Economic Entities and the Law on the Agency for Business Registration.
3. Establish a mechanism to get timely feedback from small enterprises during the implementation of the new VAT system, in order to smooth the transition to the new system and identify the critical areas.
4. Implement the laws on secured transactions and leasing, including the establishment of a collateral/leasing register and further reduce the minimum reserve requirements for foreign currency deposits.
5. Introduce a system of certification and accreditation of business advisory bodies to set standards and improve confidence in, and quality of, the services.
6. MoE and ASME should define the strategy for development of Business Incubators, working with local authorities, entrepreneur associations, universities and research centres.
7. Ministry of Education and ASME should elaborate a plan to expand the development of vocational and secondary school curricula to include introductory courses on entrepreneurship, with the direct participations of entrepreneurs and private sector associations.

## **2004 Policy Recommendations and Priorities for Action**

The 2003 EPPA report included a set of policy of recommendations for each policy dimension covered by the report, to provide inputs to policy discussion and policy making.

The 2004 EPPA Report includes a new set of policy recommendations, consisting of a number of recommendations retained from last year, selected among those that have not yet been fulfilled and are still relevant and a limited number of new recommendations, related to recent policy developments.

In addition, for each policy dimension a Priority for Action has been identified, that should be implemented over the short term (less than one year).

The implementation of the 2004 set of Policy Recommendations and Priorities for Action will be regularly monitored through the Investment Compact monitoring process and will be reviewed in detail in the EPPA 2005 report.

## **Institutional Framework for SME Policy**

### **Priority for Action**

1. The Ministry of Economy (MoE) should set a number of clearly defined and realistic milestones (as well as intermediary objectives) related to the implementation of the National SME Strategy and structure and equip ASMEE on the basis of the resources needed to reach those milestones.

## **Financial stability for ASMEE and the Regional Network**

2. The government should secure and stabilise the medium term future of ASMEE and the development of its regional network, through a mixture of national and international resources.

## **Inter-ministerial Co-ordination**

3. Implement an Inter-ministerial Group on SME Policy, co-ordinated by the Ministry of Economy and include key ministries, such as the Ministry of Finance.

## **SME data and analysis**

4. MoE and ASMEE should co-operate with the statistical office and relevant ministries in order to systematically collect statistical information, particularly for those indicators set in the 2003-2008 strategy

## **Communication with SME Stakeholders**

5. Strengthen the SME Advisory Board (SMEAB) to enable it to become a regular forum of communication and consultation with a wider range of SME stakeholders. Adequate resources are needed to make it an effective Government-SME stakeholder forum.
6. Develop the ASMEE web-site as portal for SME related information, facilitating consultation and developing links with other web-sites.
7. Use the communication channels as a two-way route, promoting feed-back on policy implementation and on the quality of the information provided.

8. Move communication tasks to local level, under central supervision, using the network of ASME regional offices.
9. ASME should develop a partnership with the Union of Employers and other private sector associations at sector and regional level to facilitate dissemination of policy information to SMEs and to receive policy inputs.

### **Rule of Law and Regulatory Environment**

#### ***Priority for Action***

10. Fully implement the new Law on Registration of Economic Entities and the Law on the Agency for Business Registration

### **Registration, De-registration, Re-registration**

11. Develop the software and introduce the system for on-line registration, planning its extension to the whole country.
12. Monitor the introduction of the single code number for each enterprise.
13. Move towards the creation of a “One-Stop-Shop” system throughout the country, as in the case of other SEE countries such as Romania (see OECD-EBRD, 2002).

### **Regulations**

14. Amend the following laws: *Law on Enforcement Procedure*, the *Law on Contracts*, the *Law on Pledge on Movable Property Entered into the Register* and the *Law on the Privatisation Agency*.
15. Develop and disseminate a check list of improvements that can be made to further eliminate, reduce or standardise the complexity of procedures for SMEs obtaining licenses, permits and certificates.
16. Set a predetermined reference time limit for each procedure.
17. Intensify the proposed reforms pioneered by the Inter-ministerial Working Group on De-regulation, in close co-operation with ASMEE and in consultation with the SME stakeholders.
18. Introduce the principle of “silent consent” as soon as practical.
19. Bring product certification standards in line with EU standards.

### **Anti-Bribery and Corruption**

20. Limit the room for the exercise of public official discretionary powers in the procedure for the issue of permits and licences.
21. Promote maximum transparency of procedures.



## Tax Policy for Small Business

### *Priority for Action*

22. Establish a mechanism to get timely feedback from small enterprises during the implementation of the new VAT system, in order to smooth the transition to the new system and identify the critical areas.

### *Policy Principles*

23. The Ministry of Finance and the Ministry of Economy, in co-operation with the ASMEE and SMEAB, should devise a system for monitoring the consistent and fair enforcement of tax laws in order to reduce unfair competition.
24. Carry out regular consultation on tax issues, with the associations representing private entrepreneurs.
25. Produce simple and up-to-date information on the tax regime for small business.

### **VAT**

26. Design the VAT refund period to facilitate cash flow, using the international standard of one month.

### *Grey Economy*

27. Use the opportunity of the introduction of VAT to launch a campaign against tax evasion and turnover under-reporting. Experience elsewhere in SEE indicates that the correct introduction of VAT, with the widest coverage possible is vital in the fight against the grey economy.
28. Strengthen efforts to collect arrears, regardless of firm size.
29. Enforce payment of social security contributions on actual salaries.

## Financial Instruments for New and Small Business

### *Priority for Action*

30. Implement the laws on secured transactions and leasing, including the establishment of a collateral/leasing register and further reduce the minimum reserve requirement for foreign currency deposits.

### *Bank-lending*

31. As a main priority, the National Bank (NBS) should further reduce the minimum reserve requirement for foreign currency denominated (forex) bank deposits.
32. Take measures to improve the access of banks to commercially-costed medium-term finance for lending, and improve the ability of banks to assess medium-term risk. Measures that would help meet these objectives include allowing banks to lend in foreign currency and creating a credit information bureau, possibly initially under the auspices of the NBS. This can put pressure on the banks to sign up for it and share information. Donor funding would be required for this purpose.

33. The credit bureau of the Banks Association of Serbia keeps records on small entrepreneurs (shops) generating an annual income of CSD 2,000,000, but it is only just becoming effective. It is recommended that the bureau be resourced to cover all SMEs and established under the auspices of the NBS.
34. Adopt regulations which would allow non-deposit credit organisations to lend to micro and small enterprises.

#### **Non-bank lending**

35. Given the extremely low level of bank lending to the enterprise sector and the even lower level of bank lending to micro-enterprises and start-ups, the central bank should allow non-depository credit organisations dedicated to lending to micro enterprises and start-ups to be set up, at least as an interim measure. The central bank does not currently allow any lending to enterprises except through banks, thereby dramatically limiting the credit available at the bottom end of the market and to start-ups.
36. The authorities should allow non-bank institutions to provide finance to the smallest entrepreneurs and to start-ups.

#### **Legal reform**

37. Pass a number of urgently required laws. These include the secured transactions law, implementation of the registry for movable and intangible collateral, completion and approval of the leasing law and implementation of a registry for leases which must be closely linked to, or possibly part of, the collateral registry.
38. Improve the regulatory conditions for taxation of leasing. Leasing as a means of providing finance for productive equipment helps enterprises in the context of unavailability of bank finance and supports the recovery of investment and production. Providing that the ruling legislation allows recovery of the asset, it substantially reduces the risks to the lessor of operating in what would otherwise be considered a volatile and difficult environment in which to do business.
39. Review the legislation on contracts and adopt the *Law on Security of Claims* to deal with the problem of creditor security

#### **Advisory Services**

##### **Priority for Action**

40. Introduce a system of certification and accreditation of business advisory bodies to set standards and improve confidence in, and quality of, the services.

#### **Quality and Accreditation**

41. Develop and publish a customer charter in each ASME regional office, setting out the range of services provided and the standards that will be adhered to.
42. Work with software developers for production of software solutions for SMEs, including libraries containing all laws and regulations affecting SMEs (there are several such products available on the market, *e.g.* "Paragraph").

### ASME and ASME Regional Network

43. ASME network should focus on the provision of basic standardised support and information services to SMEs, especially start-ups, including subsidised business support services in order to address the most evident cases of market failure. The supply of specialised services should be left to the private sector.
44. ASME should review its regional network every two years with a view to assessing sustainability and deciding how the range of services should be developed to provide best value to SMEs.
45. Strengthen agency capacity to support SMEs through the provision of resources to train existing staff and hire qualified expertise.
46. Link national and donor financial support to business centres and regional development offices, in direct relation to the quantity and quality of the services provided to SMEs. A programme evaluation scheme should be established to provide the necessary feedback.

### Representative Bodies

47. Evaluate the role of the Chambers of Commerce with regard to such issues as: nature of membership, organisational structure, linkage with government institutions (*e.g.* dissemination of information at branch level).
48. Develop synergies between the Chamber of Commerce and the ASME regional network to spread the provision of basic services to SMEs.

### Business Incubators

#### Priority for Action

49. MoE and ASME should define the strategy for development of Business Incubators, working with local authorities, entrepreneur associations, universities and research centres.

50. Start developing adequate legal and other regulations for the work of Business Incubators.
51. ASME should build an alliance to develop the business incubators programme from a pilot to a fully fledged programme.
52. The benefits of Business Incubators, such as lower initial fixed costs, better inter-company communication, closer synergies with clients and suppliers should be promoted to entrepreneurs.
53. Focus initially on a limited number of sectors, such as the food production and processing industry, and the ICT sector.

### Entrepreneurship, Vocational Education and Access to Technology

#### Priority for Action

54. Ministry of Education and ASME should elaborate a plan to expand the development of vocational and secondary school curricula to include introductory courses on entrepreneurship, with the direct participations of entrepreneurs and private sector associations.

55. Government should design a programme with the goal of promoting the adoption of new technologies and improving technical capabilities in SMEs.
56. An entrepreneurship awareness campaign should be put in place with the aim of encouraging more entrepreneurship and highlighting the benefits to society and individuals with the resulting generation of employment.
57. Enact regulations to harmonise technical standards in educational services used by SMEs with EU standards.
58. Promote in-house management, and technical training programmes and internships for young people.

## *Part II*

### *Chapter I*

#### **VIEWS OF THE SME OWNERS AND MANAGERS**



## 1. Introduction

This section contains the analysis of the results of the focus group research on seven dimensions of good practice for the SME business environment. The analysed data were collected from the SME focus groups and experts in March and April 2004 and the questionnaires completed by the participants. The research conducted in 2004 includes the opinions of entrepreneurs and experts on an additional new dimension of *Good Practice - Entrepreneurship, Competition, Access to Technology*, as well as the opinions on targets relating to the implementation of the EU Charter for Small Enterprises. This was not included in the March 2003 EPPA report for Serbia thus limiting comparison. In addition, some of the questions have been amended and are not directly comparable with the questions in the previous study. In these cases no comparison is given.

The analysis of the SME business environment is made on the basis of assessment of the following seven dimensions of good practice:

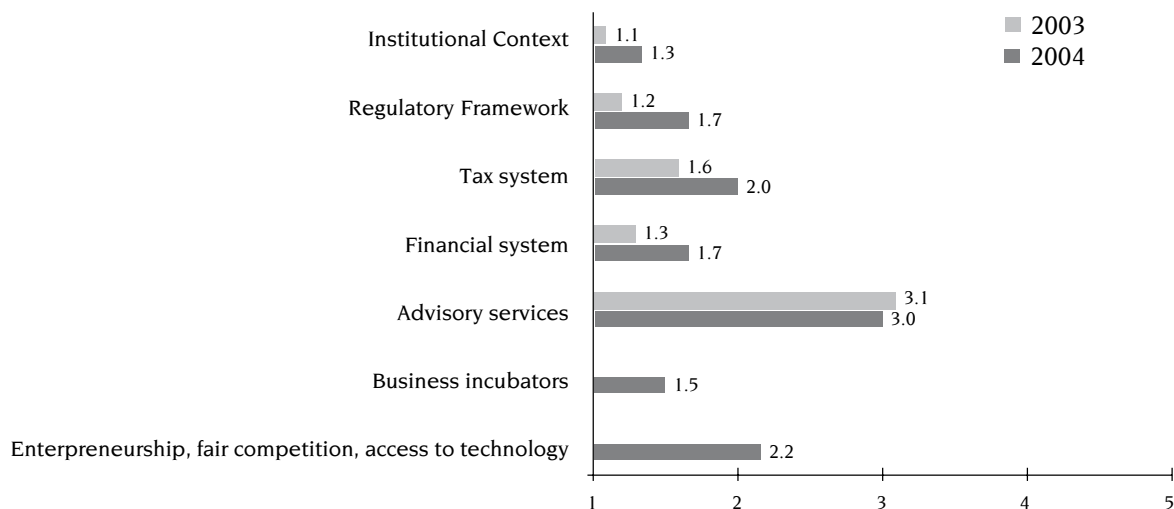
- Institutional framework for SME policy
- Rule of law and regulatory environment
- Tax policy for small businesses
- Financial instruments for new and small businesses
- Advisory services for new and small businesses
- Business Incubators
- Entrepreneurship, fair competition, access to technology (and targets related to the implementation of the European Charter for Small Enterprises in the Countries of the Western Balkans – Serbia)

The questionnaire served as the basis for discussion by focus group participants and experts and was subsequently completed individually by them. The questionnaire consisted of two groups of questions; one set comprising of yes/no questions, and the other comprising questions in which participants gave ratings on a scale of 1 to 5: **1 = very poor, 2 = poor, 3 = satisfactory, 4 = good and 5 = very good**. At the beginning of the analysis of each of the seven dimensions of good practice, we present the average results of the participants' ratings on the particular dimension.

The average ratings of dimensions of good practice in the 2003 EPPA report (OECD, March 2003, p.17) and 2004 for each of the seven dimensions are presented in Figure 1-1 below. This analysis indicates a slight improvement in the SME business environment compared to the previous report. In the previous report, the average ratings given for all dimensions were close to “very poor”, with the exception of *advisory services*, which were assessed as “satisfactory” both this time and previously.

The views of the SME owners and managers, who participated in the focus groups in 2004, on the other dimensions of good practice were slightly better when compared to the average of the opinions expressed in 2002, but are still generally in the range “very poor” to “poor”. This is confirmed by the general view expressed during the focus group discussions that not much progress has been noticed in most of the dimensions of good practice in the past year or so. Exceptions were in the areas of the image of entrepreneurs, quality of education and access to technology. SME participants agreed that improvements in these areas were made over the previous year. Although the practice of using Business Incubators (BIs) has not developed in Serbia (with the exception of one private Business Incubator in the area of ICT), some entrepreneurs knew what Business Incubators involve and agreed that they had significant potential to help the development of the SME sector in Serbia.

**Figure 1.1. Average Ratings by SME Owners and Managers of the Seven Dimensions of Good Practice, 2003 and 2004**

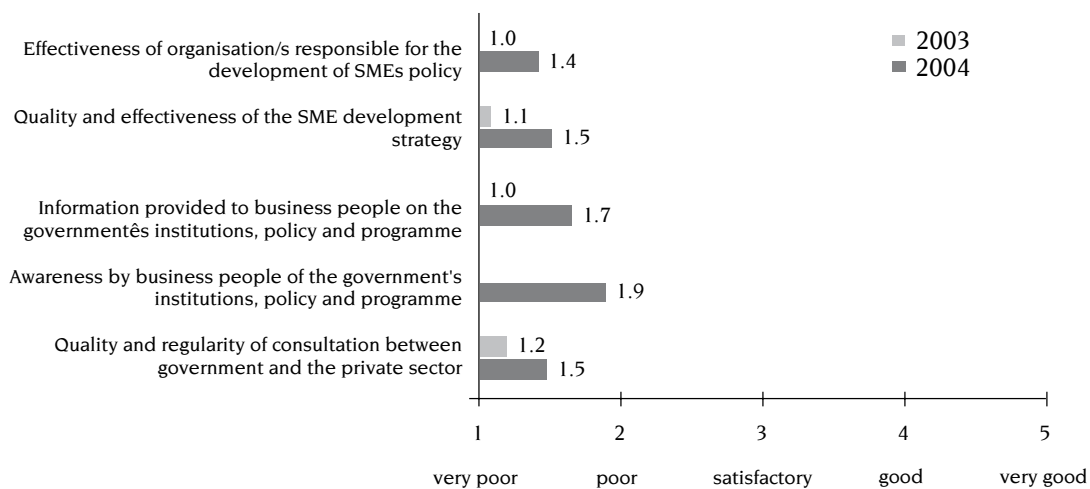


## 2. Institutional Framework for SME Policy

The following issues were researched under this heading:

1. Clear assignment of organisational responsibility for the development of SME policy.
2. The effectiveness of organisation/s in developing an environment to encourage entrepreneurship and the development of SMEs.

**Figure 1.2 Average Ratings for the Institutional Framework Questions, 2003 and 2004**





3. Awareness of SME development strategy and the quality and effectiveness of the SME development strategy.
4. The local and regional governments' mandate and resources (funding, people and skills) to promote SME development.
5. The information provided and awareness by business people of the Government's institutions, policy and programmes to support new entrepreneurs and develop existing SMEs.
6. Awareness of consultations between Government and the private sector on SME policy.
7. The quality and regularity of consultation between Government and the private sector on SME policy and its performance and assessment.
8. The performance of government institutions in supporting small business since March 2003.

### Organisational Responsibility

All the average ratings by focus group participants on the institutional framework for SME policy in 2004 range between "very poor" and "poor". However, this is a significant improvement on 2002 when the ratings were generally close to "very poor". The overall average rating (see figure 1.1) has improved to 1.3 from 1.1, but still remains very close to an average of "very poor". The overall perception is of some limited progress in terms of building the institutions which provide a more favourable environment for SMEs operations.

	2004	2003
1. Do you know if a clear <b>organisational responsibility</b> for the development of SME policy has been assigned by Government?	Yes: 53.3% No: 46.3%	n/a

Over half of the participants know about the institutions designated by government for the development of SME policy. However, many are of the opinion that the measures pursued by government or relevant ministries mainly help the start up and development of SMEs in the larger towns, and the further the distance from the larger towns the weaker the impact.

*"SME development policy has been institutionalised, but the existing institutions still do not encourage SME development in an appropriate way."*

### Effectiveness of Government Organisation

	2004	2003
2. How do you rate the <b>effectiveness of the organisation/s</b> in developing an environment to encourage entrepreneurship and the development of SMEs?	1.4	1.0

Nearly half of participants assessed the effectiveness of the relevant Ministry and Agency as "poor", with an average rating of 1.4 *i.e.* between "very poor" and "poor". The main reason for the assessment given by the focus group participants is political instability, which they believe has reduced the attention paid to the development work with SMEs. Also, entrepreneurs are of the opinion that officers employed in state institutions have insufficient skills and seem uninterested in solving the real problems of the SME sector.

*"The bureaucracy is outdated, which does not necessarily mean that it is automatically bad, but it is certainly incapable of applying new solutions."*

**SME Development Strategy**

	2004	2003
3. Do you know if a government SME development <b>strategy</b> exists?	<b>Yes: 30%</b> <b>No: 70%</b>	<b>n/a</b>

3.1 How do you rate the <b>quality and effectiveness of the SME development strategy</b> ?	2004	2003
Overall	<b>1.5</b>	<b>1.1</b>
Quality	<b>1.7</b>	<b>n/a</b>
Effectiveness	<b>1.4</b>	<b>n/a</b>

Most of the focus group participants do not know that the Government of Serbia has an SME Development Strategy. The quality of this Strategy has an average rating of 1.7 *i.e.* below “poor” and its effectiveness at 1.4 *i.e.* closer to “very poor”. Because such a small proportion of participants know about the strategy, the consultants who undertook the focus group work believe that the assessment actually expresses a general view about the government’s commitment to the SME sector. They believe that the participants see the Strategy as something that may exist, but as a ‘dead letter’, and not as a document which helps in a practical way in the development of their businesses.

*“Everything may be nicely defined in that paper, but in practice SMEs are left to their own resources.”*

*“Even if such a strategy exists, it is not applied in practice. It allows, for example, that foreign textile goods enter customs duty-free with their dumping prices and imperil the competitiveness of domestic manufacturers”.*

**Local and Regional Government**

	2004	2003
4.1 Do <b>local and regional government</b> have the mandate to promote SME development?	<b>Yes: 26%,</b> <b>No: 48%</b>	<b>n/a</b>

Many of the participants (48%) think that the regional and local authorities have no mandate to promote SME development, while an additional 24% are not sure.

	2004	2003
4.2 Do <b>local and regional government</b> have the resources (funding, people, and skills) to promote SME development?	<b>Yes: 22%</b> <b>No: 62%</b>	<b>n/a</b>

Just under two-thirds of participants (62%) are of the opinion that local and regional authorities do not have resources (funding, people and skills) to promote SME development, while 16% of them were unable to answer this question.

*“Local authorities have neither the mandate nor the resources, they lack initiative and accuracy, and they are not good at their work. What often happens is that presidents of municipalities make decisions on the distribution of credits and donations on the basis of political criteria.”*

### Information Provided and Awareness of Government Programmes

5.1 How do you rate the <b>information provided</b> by business people of the government's institutions, policy and programme to support new entrepreneurs and develop existing SMEs?	<b>2004</b>  1.7	<b>2003</b>  1.1
5.2 How do you rate the <b>awareness</b> by business people of the government's institutions, policy and programme to support new entrepreneurs and develop existing SMEs?	<b>2004</b>  1.9	<b>2003</b>  n/a

The average assessment on information provided on government institutions, policy and programmes to support new entrepreneurs and develop existing SMEs in 2004 has improved (1.7) since last year's (1.0), but it is still on average regarded as less than "poor". Awareness of the institutions, policy and support programmes for new and existing SMEs is also deemed to be "poor" (1.9). The answers are consistent, as the access to information is the basic condition for an entrepreneur to be aware and able to effectively avail of the services provided by the state institutions in charge of small business development.

***"Business peoples' knowledge of government institutions is very poor at all levels. Business people get information much faster through the media than through government services, and these services often do not present such information in its original form."***

### Consultations between Government and the Private Sector

6. Are you aware of <b>regular consultations</b> between government and the private sector?	<b>2004</b>  Yes: 12.2% No: 87.8%	<b>2003</b>  n/a
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Most (87.8%) of the focus group participants know nothing about regular consultations between government and the private sector.

7. How do you rate the quality and regularity of <b>consultation between government and the private sector</b> on SME policy and its performance and assessment?	<b>2004</b>	<b>2003</b>
Overall	1.45	1.2
Quality	1.5	n/a
Regularity	1.4	n/a

SME owners and managers rated the quality and regularity of consultations on SME policy and its performance and assessment between government and private sector as being between "very poor" and "poor" (average ratings 1.5 and 1.4 respectively). They are of the opinion that government needs to discuss these issues with entrepreneurs. They believe that this would facilitate the enactment of laws that are more likely to create a supportive environment for SMEs and consequently better development and growth.

## Changes in the Institutional Framework

8. How do you rate the <b>performance of government institutions</b> supporting small business since March 2003?	2004		
	Worse 28.8%	No change 61.2%	Better 10.0%

10% of focus group participants are of the opinion that the performance of government institutions has improved, but 61.2% believe that there has been no change in the performance since March 2003.

### 3. Rule of Law and Regulatory Environment

The following issues were researched under this heading:

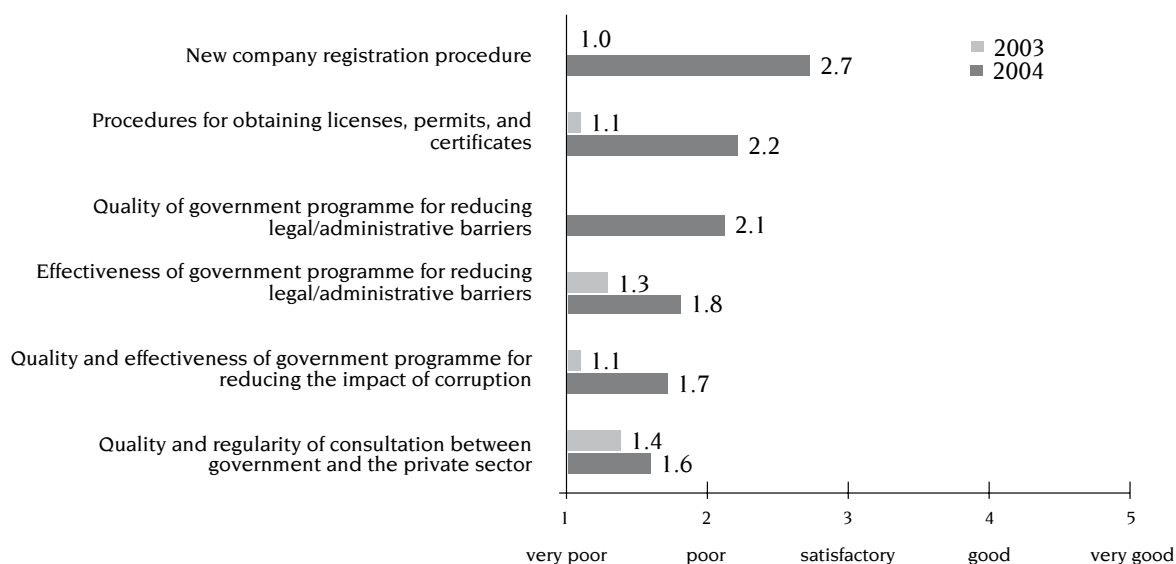
1. The formalities for new company registration and comments on the process
2. The procedures for obtaining licenses, permits and certificates necessary for business operations
3. The existence of a Government approved programme for reducing the legal/administrative barriers for business and rating of the quality and effectiveness of this programme
4. Awareness of Government approved programmes for reducing the impact of corruption
5. The quality and effectiveness of the programme for reducing the impact of corruption
6. The quality and regularity of consultation between Government and the private sector/SME policy community on draft legislation and regulations that affect business.

Results of the research showed the following:

- The quality and regularity of consultations between government and entrepreneurs on the drafting of new laws and regulations are still poor.
- Most entrepreneurs are of the opinion that the administrative barriers to registration and business operation of companies have not yet been fully removed, but the reduction of administrative barriers and procedures is moving in the right direction.

Overall the regulatory environment for small business is perceived by SME owners and managers to have improved to an average of 1.7 compared to 1.2 in last year's report (see figure 1.3).

**Figure 1.3 Average Ratings for the Regulatory Framework Questions, 2003 and 2004**



## Company Registration Process

	2004	2003
9. Please comment on the formalities (number of steps, time needed, and cost) for <b>new company registration (certification of existence)</b> .	2.7	1.0

The overall process of registration of a new company is assessed by most of focus group participants as now nearly satisfactory (average rating 2.7). This represents a significant improvement from last year when the consensus was the process was then far too complicated, costly and bureaucratic.

*“I had to do registration pursuant to the new Urban Planning Law. A pleasant surprise – I finished it in only one day.”*

Participants in the focus groups stressed that the number of documents necessary for registration has been reduced, but the time needed for this procedure still varies, depending on the judge in charge. They said that the commercial courts do not hold the updated register of names of the existing companies. The result is that in cases where an entrepreneur wishes to register a company name that already exists, he is required to recommence the whole registration procedure from the beginning. This involves the entrepreneur modifying all the documentation concerned and if necessary having it notarised again. Such cases, lead to significantly increased registration costs. However, the *Law on Registration of Economic Entities* enacted in May 2004 will resolve this problem by introducing a unique central electronic database on all economic establishments. This Law requires that the economic court send all its documentation and electronic database information on economic entities to the Agency for Economic Registers by March 15, 2005 at the latest.

Entrepreneurs supported the establishment of the agency for company registration in order to simplify the registration procedure and reduce costs by as much as possible. There was a proposal for the introduction of the concept of guarantor, *i.e.* a partner-company possessing assets of a certain value which could act as a guarantor for a new start up company. This proposal results from some participants' negative experiences of doing business with companies that were insolvent and were subsequently closed by their owners without having fulfilled their obligations to suppliers. The “Guarantor” in this case would be obliged to pay the suppliers for the delivered goods/services, if the enterprise for which it gave guarantee at registration was closed.

## Procedures for Obtaining Necessary Licenses, Permits and Certificates

	2004	2003
10. Please comment on the procedures for obtaining <b>licenses, permits, and certificates</b> necessary for business operations.	2.2	1.1

The overall procedure for obtaining licenses, permits and certificates necessary for business operations has improved from “very poor” last year (1.1), but is still regarded as only slightly better than “poor” (2.2). Participants pointed out that in addition to the need for licenses for certain business activities (dairy and meat production, construction, *etc.*), specialists holding certain positions in a company also need to have licenses. The consensus was that obtaining a personal license is too costly when compared to the salaries of some specialists. It was suggested that licenses should be issued routinely at minimum cost on the basis of specific references and qualifications.

*“The procedures for obtaining licenses, permits and certificates are still too complicated, bureaucratic and costly”.*

The new *Law on Planning and Construction* introduced the facility for the *Engineering Chamber of Serbia* to issue personal licenses in the field of civil engineering made out to an individual engineer. If the enterprise is entered in the Civil Engineering register, if it employs engineers with the license for responsible provision of works and if it has adequate professional experience in constructing buildings of a certain type and purpose, it can undertake the construction of these buildings. Whether the criteria are fulfilled or not is established by an authorised minister, based on the recommendation of an expert committee that he creates for this purpose. No licenses have been issued to companies on this basis as yet.

Most of the participants in the focus groups expressed their dissatisfaction with this approach. In their opinion, it would allow a situation where there is the possibility of a person possessing this type of license being employed part-time on several projects. They believe changes and supplements to the *Law on Planning and Construction* should be made to simplify the issue of acquiring licenses for enterprises.

*“Opinions are divided, from discontent with the way in which the question of the issuance of licenses and permits was regulated, to the conclusion that the mafia rules in this area both at local and national level.”*

#### Programme for Reducing Administrative Barriers

	2004	2003
11.1 Are you aware of a <b>government approved programme for reducing legal/administrative barriers</b> for business?	Yes: 22% No: 78%	n/a

Most of the participants (78%) are still not aware of the government programme for reducing legal/administrative barriers to SME business operations.

	2004	2003
11.2 How do you rate the <b>quality</b> and <b>effectiveness</b> of this programme?		
Overall	1.9	1.1
Quality	2.1	n/a
Effectiveness	1.8	n/a

The results are consistent with a separate 2003 study of all factors in the business environment which affect business operations. The factor “**state officials’ sensitivity to business**” was given the lowest rating (1.96) on a scale from 1 to 5 (G 17 Institute, September 2003, p. 145).

*“Certain positive developments have taken place in terms of removing administrative barriers to business, but it is still not sufficient”.*

SME owners and managers participating in the focus group research acknowledged that the government has liberalised certain areas (exporting and importing), but problems remain with customs both in terms of exports and imports. They also stressed that Serbia is extremely bureaucratic and keeps unnecessary parallel records.

*“Plenty of time is wasted on the collection of the documentation required for obtaining the license, for each paper you have to pay a fee, and there is also the bribe on the top of everything. It would be much more efficient if all these activities were completed by one institution through departments at local level.”*

## Programme for Reducing the Impact of Corruption

	2004	2003
12. Are you aware of government approved programmes for <b>reducing the impact of corruption</b> ?	Yes: 71.4% No: 28.6%	Yes

Most of the participants are aware of government measures for combating corruption.

*“It seems that some progress has been made, but corruption is still present, especially in construction. The state apparatus is too unwieldy, and you still need to have personal contacts to finish some things. You often don’t know who to offer the money to in order to ensure the completion of what you need”*

13. How do you rate the quality and effectiveness of this programme?	2004	2003
Overall	1.8	1.1
Quality	2.0	n/a
Effectiveness	1.5	n/a

The quality of programmes for combating corruption is still regarded as “poor”. The effectiveness of the programme was regarded as being even worse. It averaged between “very poor” and “poor”. The enforcement of the new *Public Procurement Law* was especially criticised. The participants said that there are numerous deviations from and abuse of basic intentions of this law.

*“It is too early for an assessment of quality. Efficiency does not show because of the lack of co-ordination between state authorities and public enterprises which provide services for business operations (water supply, postal and telephone services, power supply, heating).”*

## Consultation between Government and the Private Sector

14. How do you rate the <b>quality and regularity of consultation</b> between government and the private sector/SME policy community on <b>draft legislation and regulations</b> that affect business?	2004	2003
Overall	1.6	1.4
Quality	1.6	n/a
Effectiveness	1.6	n/a

SME owners and managers assessed the quality and regularity of consultations between government and the private sector on draft legislation and regulations that affect business as being between “poor” and “very poor” (with average ratings 1.6). This rating is slightly better than that of last year’s research (1.4). The consultation process with SMEs, organised by government, has not achieved a satisfactory level.

*“Government is not interested in consultations. Laws are not clear and precise. Enforcement thereof requires interpretation. Consultants create bad draft laws in order to interpret them subsequently. What is lacking is the monitoring of the enforcement of laws.”*



## Changes in Regulatory Framework

14.1 How do you rate the change in the regulatory environment (registration, licenses, and permits) since March 2003?	2004		
	Worse	No change	Better
	6.8%	70.5%	22.7%

Nearly a quarter of participants said that the changes implemented have improved the regulatory environment. However, most are of the opinion that the situation in relation to the registration of companies, issuance of permits, certificates and licenses is unchanged.

The slow pace of amendment to laws is resulting in a growing impression that the economy is “*in permanent change*”. While expecting change for the better, SME owners and managers do also have a great need to operate under “*stable conditions*”. What frustrates them most is that many changes to new regulations are found to be ill-defined and poorly planned, causing unnecessary problems at the implementation stage. There is also a high degree of frustration with the perceived unequal application of regulations and non-compliance by many economic actors.

***“These amendments failed to resolve problems with regard to the re-registration of indebted companies. SMEs’ registration should be made dependant on the bringing of certain assets or guarantees into the company for the sake of collection of debts by creditors.”***

## 4. Tax Policy for Small Businesses

The following issues were researched under this heading:

1. Whether the present tax policy encourages new enterprise and the rating of the tax system in terms of the encouragement, support and ease of use that it provides to new and existing SMEs.
2. The stability and transparency of the tax system for small enterprises.
3. Percentage of net profits SMEs typically pay in tax.
4. Consultation and communication between Government and the private sector on tax rates and incentives for enterprises.
5. Consistency of tax policy with other Government policies.
6. Change in the taxation regulatory environment.

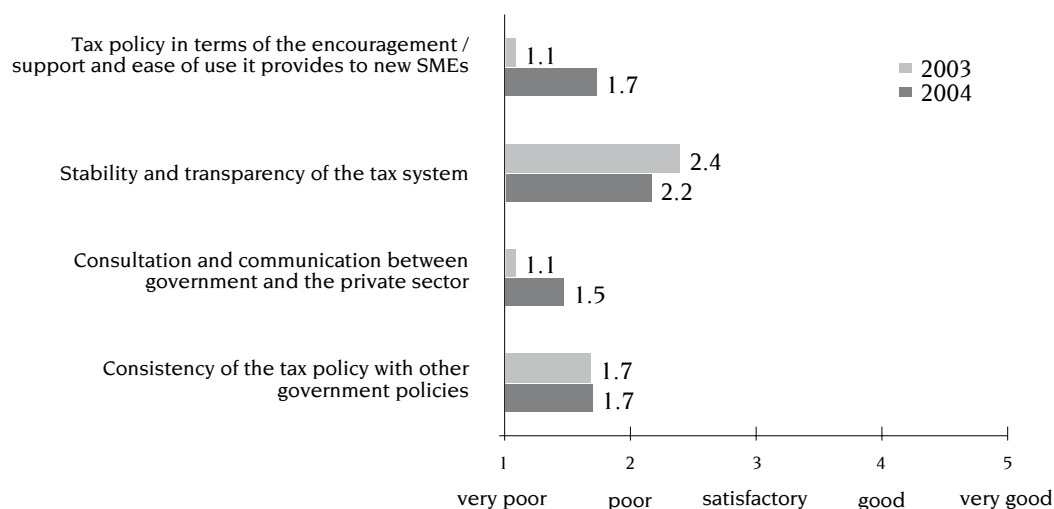
In the period between March 2003 and February 2004 no tax policy changes were made. However, the new government, which came to power in February 2004, has initiated a series of changes in tax policy with a view to encouraging small business. The preparation of new regulations took place in March 2004, around the same time as the focus group meetings were being held and the questionnaires completed. The wage bill tax was revoked. This had placed a significant burden on labour-intensive activities. The Ministry of Finance has drafted the *Law on Amendments and Supplements to the Law on Corporate Income Tax*. This will significantly improve conditions for the operation of SMEs, because the corporate income tax rate will be reduced from 14% to 10%.

Because of an expected budget deficit in 2004, Government is introducing selective increases in tax duties aimed at wealthier personal tax payers (G17 Institute Economic Review, 48–49/2004, p.21).

In discussions, the indications of changes in tax policy aimed at creating considerably better conditions for SME operations were very positively received by focus group participants. Overall, the rating of tax policy has improved from being on average regarded as between “very poor” and “poor” (1.6) in the previous study to an average of 2, i.e. “poor”, this year (See figure 3.1 above).



**Figure 1.4. Average Ratings for the Tax System Questions, 2003 and 2004**



With regard to tax policy as a whole, focus groups put the main emphasis on the following:

### Encouragement of Enterprises

	2004	2003
15. Does the present <b>tax policy encourage new enterprise?</b>	<b>Yes: 16.3%</b> <b>No: 83.7%</b>	n/a

Most participants are of the opinion that the present tax policy does not yet encourage new enterprise.

The average ratings of the impact of tax policy on starting up new SMEs have improved to 1.7 from the “very poor” (1.1) rating in the previous study. However, since no changes were actually made in tax policy last year, it is believed that the assessment results more from the announced changes in tax policy by the new Government and expected improvement rather than actual improvements already made. Owners of construction companies, for example, are in favour of the announced tax measures:

*“Citizens are exempt from the 20% tax if they enter into a contract with a company possessing a technical design and construction license, if project documentation is available, equipment obtained and installed by the company.”*

Focus group participants highlighted examples of unequal application of tax instruments on companies with different types of ownership:

*“With regard to outsourcing, when a private company is providing a sewing service for another entity, it has to pay tax on the service, while a socially-owned enterprise which provides the same service to a non-resident entity is not burdened with such a tax.”*

It must be pointed out that socially-owned companies in Serbia employ workers who carry out the sewing within the enterprises, so there is no actual turnover.

***“A typical example of the lack of coordination between these institutions is that financial police work separately from the courts and do not punish a company that is not registered for the activity it performs and for purchasing goods.”***

Focus group participants also highlighted the unfair position for companies properly registered with regard to the grey economy.

***“...the one who works and employs 50 or more registered workers cannot be competitive with those who don't register their workers, because the former is paying all obligations, while the latter doesn't have to do so.”***

***“The tax rate on reproduction material and finished products is almost equal. In such conditions I can't be competitive with the company importing finished products from Turkey.”***

Focus group participants said they feel as though SMEs are the only businesses fully paying their fiscal obligations. They believe that there are many enterprises, particularly the state-owned and larger companies, in Serbia that have not paid anything for years. They believe that the government has done little to resolve this inequity.

The revocation or reduction of certain taxes has proved to have a positive impact on the reduction of the grey economy. For example, when the tax on computers and software was scrapped at the beginning of 2003, the grey market in this area was considerably reduced. SME owners and managers are of the opinion that trading in excise product on “flea” markets should be banned because of the unfair competition it creates.

#### **Tax Policy in Terms of the Encouragement/Support to SMEs**

	<b>2004</b>	<b>2003</b>
<b>15.1 Rating given to the tax policy in terms of the <b>encouragement/support</b> that it provides to new and existing SMEs.</b>	<b>1.7</b>	<b>1.1</b>

The average rating given to tax policy in terms of the encouragement/support to new and existing SMEs is 1.7, which is an improvement compared to last year (1.1).

Focus group participants said that the tax policy in Serbia at its present stage needs to have a pronounced emphasis on development, with a focus on the development of SMEs. Participants also expressed the opinion that the proportion of profit which is invested in the development of the company and which creates new jobs should be entirely tax-exempt. They also believe that the personnel performing operational tasks in tax administration need training. They said particular problems are caused by administrative and desk clerks who resist adapting to change.

Participants from Southern Serbia said tax administrative officials did not inform them that start-ups were exempt from corporate income tax in the first year of work and said that it is difficult to get the authorities to reimburse overpayments.

***“...and I was due money back, but didn't yet receive it. It is much easier for them to collect than to return.”***

This “*one way*” attitude is very detrimental to SMEs’ perception of the tax system.

### Tax Policy in Terms of the Ease of Use

	2004	2003
15.2 Rating given to the tax policy in terms of the <b>ease of use</b> that it provides to new and existing SMEs.	1.8	1.1

The ease of use of tax policy for new and existing SMEs is perceived as having improved. The average rating by focus group participants is now 1.8 *i.e.* “poor”, up from the previous “very poor”. The situation will obviously not improve further until the tax policy and system changes planned are fully implemented, in particular in terms of the reduction of the number of instruments, simplification of procedures, and education of tax administration staff and company staff responsible for financial issues. In this context participants complained about the delay in introducing the VAT system, which had again been postponed for a year to January 2005. They also said that improved coordination in defining tax and customs policy for small businesses is necessary, especially coordination between the Ministry of Finance, the Ministry of Economy and Privatisation and the Ministry of International Economic Relations.

SME owners and managers are of the opinion that the tax system needs to be computerised and that the number of papers required for tax filing and payment reduced.

A particular problem highlighted is the issue of social insurance contributions which, according to law, have to be calculated on the basis of the mandatory minimum wage, regardless of whether the employee's wage is lower than the mandatory minimum. This is a heavy burden for companies which have many employees whose wages are lower than prescribed tax and contribution base and for companies paying wages twice a month.

### Tax System Stability and Transparency

	2004	2003
16.1 Rating given to the <b>stability of the tax system</b> for small enterprises.	2.2	2.4

The average rating given by focus group participants to the stability of the tax system for small enterprises is slightly lower than last year's (2.2 compared to 2.4), *i.e.* it is closer to the descriptive rating “poor”. Participants highlighted the fact that many companies have registered only for the purpose of money laundering and these companies are very difficult to detect. These so called “phantom” companies are a legacy from the past, having emerged in reaction to economic sanctions imposed by international community to FR Yugoslavia. They distort the statistics on the creation of real new businesses and a determined effort needs to be made to eliminate them from reported statistics. This may involve direct surveying of companies each year rather than just relying on data from registrations.

	2004	2003
16.2 Rating given to the <b>transparency of the tax system</b> for small enterprises.	2.1	2.4

The average rating given to the transparency of the tax system for small enterprises is 2.1, which is close to “poor”.

**Percentage Share of Taxes in SMEs' Annual Net Profits**

17.1. What percentage of annual net profits do SMEs typically pay in tax?	2004			2003
	30% 10-15%	24% 15-20%	46% no reply	n/a

Focus group participants gave different answers to the question of what percentage of annual net profits SMEs typically pay in tax. 30% of them said that this percentage ranges between 10 and 15%, while 24% of them said between 15% and 20%.

17.2. Is it <b>increasing</b> / <b>decreasing</b> ?	2004			2003
	34%: increasing	26%: decreasing	30% no reply	n/a

A third of the participants said that the share of taxes in annual net profits had increased, while a quarter said that the share had decreased.

**Consultation and Communication on the Tax Policy Measures**

18. Rating given to the <b>consultation and communication</b> between government and the private sector on tax rates and incentives for enterprises.	2004	2003
	1.5	1.1

The consultations and communication between governments and the private sector on tax rates and incentives for enterprises had slightly improved in 2004 (1.5) compared to 2003 (1.1).

In spite of the limited improvement, the situation in relation to communication between the state authorities and SMEs is still regarded as rather poor. Consultations about the determination of tax rates for enterprises are rare.

**Consistency of the Tax Policy with Other Government Policies**

19. Is the <b>tax policy consistent with</b> other government policies aiming at improving the operational environment for small business?	2004	2003
	1.7	1.7

Focus group participants believe consistency of tax policy with other government policies aiming at improving the operational environment for small business is below "poor", with the average rating of 1.7.

## Changes in Tax Environment

20. Rating given to the <b>change in the tax environment</b> since March 2003?	2004		
	Worse 18%	No change 70%	Better 12%

The majority of participants thought that there had been no change in the tax environment since March 2003. A relatively small proportion of participants said that situation has improved. This is consistent with the fact that the proposed changes were only announced by the new government this year.

## 5. Financial Instruments for New and Small Businesses

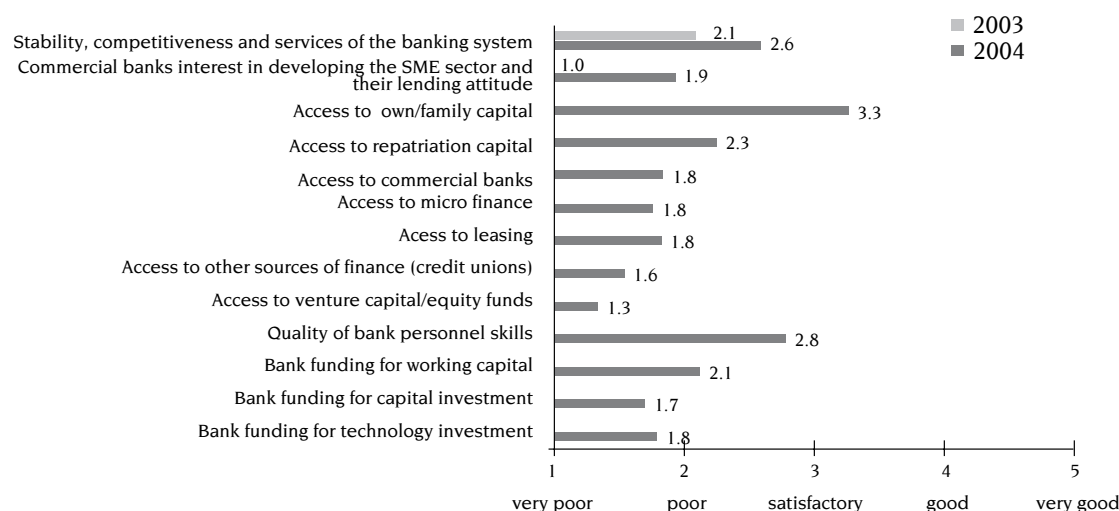
The following issues were researched under this heading:

1. The stability, competitiveness and services of the banking system.
2. The commercial banks' interest in / attitude towards extending credits to the SME sector and their lending attitude with respect to the SME sector.
3. The SME access to the following main sources of finance:
  - Own/family capital
  - Repatriation capital (from family / friends abroad)
  - Commercial banks
  - Micro finance
  - Leasing
  - Venture capital/Equity
  - Others (*e.g.* credit unions)
  - Bank personnel skills.
4. The availability of funding for
  - Working capital
  - Capital investment
  - Technology investment

Change in the banking environment since March 2003 for

- Provision of services and
- Lending

**Figure 1.5. Averages Ratings for the Financial System Questions, 2003 and 2004**



The overall average ranking increased slightly since the previous study (to 1.7 from 1.3 - see Figure 3.1). However, SME owners and managers said at the focus group meetings that the banking system is poor in its support for SME development. They believe that SMEs require a different system of financing from the one for big companies. They expressed mixed views about the quality of the banking sector and the transparency of the conditions it applies. While some doubts were expressed at the effectiveness of the financial markets, it was acknowledged that the situation is improving.

### Stability, Competitiveness and Services

21. How do you rate the <b>stability, competitiveness and services of the banking system?</b>	2004	2003
Overall	2.6	2.1
Stability	2.7	n/a
Competitiveness	2.7	n/a
Services	2.5	n/a

The general view of focus group participants is that the stability, competitiveness and services of banks and the banking system is now close to "satisfactory". Many commented that the banks in Serbia are oriented toward bigger companies or toward safer and more profitable activities and do not understand SME needs. The dissatisfaction is partially focused on foreign banks. They are seen to operate to the standards of their native countries, which are much stricter than the standards of local banks.

SME owners and managers think that interest rates are too high, which is true given the inflation rate. However, for interest rates to be lower, it is accepted that as well as reducing inflation, it will be necessary to ensure that the legal system provides full protection for creditors, thus reducing the risk premium in interest rates (G17 Institute Economic Review, 28/2002, p. 20).

*"The banking system is stable. However, the domestic banks are not competitive; they have interest rates that are too high. Foreign banks are very conscious of the profitability of investments they credit and their procedures are shorter."*

*"The most difficult thing is to obtain the first credit."*

During the focus group discussions, mixed opinions were expressed about the number of banks. Some participants are of the opinion that the existing economic situation is more favourable for banks, and consequently their number is growing. Some foresee enlargement of banks as a result of economic expansion. Others, on the other hand, believe that there are not enough banks outside the main cities.

*"Companies located in towns and municipalities which don't have their own banks face more problems communicating with banks than companies from Belgrade, where, as a rule, all banks have their registered offices."*

### Commercial Banks' Interest in Developing the SME Sector

22. How do you rate the commercial <b>banks interest in developing the SME sector?</b> And the <b>lending attitude</b> of the commercial banks to the SME sector?	2004	2003
Overall	1.95	1.0
Interest	2.0	
Lending attitude	1.9	

While there has been an improvement from the “very poor” rating of the last study, focus group participants still believe that the commercial banks’ interest in development of the SME sector and their lending attitude to the SMEs sector is “poor” (average rating 2.0 and 1.9 respectively). They believe that, based on past experiences in Serbia, banks are not really interested in financing SMEs without guarantees because investments are considered too risky and there is insufficient profit to be made on these types of loans.

***“The procedure for getting mortgages is lengthy and expensive.”***

Often real estate is not entered in the land registers leading to problems with mortgages.

***“There is interest on the part of banks in lending to SMEs, providing that SMEs have guarantees or a mortgage. There is a problem, however, in registration of real estates in the land registers. This is the key obstacle which needs to be removed.”***

## Access to Finance

### 23.1 Rating of access to the various main sources of finance

**Table 1.1 Relative Importance of Main Financial Sources Accessed by SMEs**

Financial Sources	2004 Rating	2004 Ranking	2003 Rating
Family or own capital	3.26	1	n/a
Repatriation capital	2.25	2	n/a
Commercial Banks	1.84	3	n/a
Leasing	1.83	4	n/a
Micro-finance Funds	1.76	5	n/a
Others (e.g., credit unions)	1.55	6	n/a
Venture/Equity/ Development Funds	1.34	7	n/a

The main source of SME financing is own/family capital and repatriation capital (from family and friends). Other forms of financing (commercial banks’ loans, leasing, credit unions and development funds) are still far less significant. In conditions of money shortage and an undeveloped financial market, a very risky form of financing is being used by the suppliers - they are bringing in business partners. The result of this form of financing is chronic non-liquidity of the economy and an inevitable lack of financial discipline.

***“One’s own capital is the only stable and the best source of financing for SMEs. You can borrow from business partners, relatives, friends, from foreign credit lines, but very rarely from commercial banks.”***

A number of entrepreneurs are not willing to use their property as collateral for obtaining loans.

***“Loans are very unfavourable. To get a loan of about €6,000, you need to put a mortgage on a house worth €100,000, with 2% monthly interest, plus about €200 to be paid to the judge to certify the contract.”***

Leasing is used by entrepreneurs whose businesses are more developed.

***“...Leasing in the construction business is a very good method of financing, because machines and equipment are expensive.”***

Some entrepreneurs managed to obtain loans from the Development Fund of the Republic of Serbia, but this Fund gives only limited short-term loans.

*“In the Development Fund of the Republic of Serbia, they have the strategy to distribute the money they dispose of into as many loans as possible, to ensure its maximal utilisation. This is more micro financing”.*

### The Quality of Banking Personnel Skills

	2004	2003
23.2 Rating of the quality of bank <b>personnel skills</b> .	2.8	n/a

Participants assessed the quality and skills of bank personnel as nearly “satisfactory” (with average ratings 2.8).

*“If you have the necessary documents (confirming title, deeds on facilities and machines), bank officers are obliging and efficient.”*

### Bank Funding for SMEs

24.1 How do you rate bank funding for: working capital; capital investment and technology investment?

**Table 1.2 Relative importance of different purposes of Bank Funding Accessed by SMEs**

Bank Funding	Rating	Ranking
Working capital	2.1	1
Technology Investments	1.8	2
Capital Investments	1.7	3

Focus group participants are of the opinion that banks are more willing to give loans to SMEs for working capital. Many entrepreneurs stressed that they had only managed to survive and develop their businesses by only using loans for working capital which they obtained from foreign banks.

*“If you have a business plan on the basis of which the bank could justify the investment, you may be granted a desired credit for working capital, providing that you have necessary guarantee.”*

### Change in the Banking Environment

24.2. Rating given to the <b>change in the banking environment</b> for SMEs since March 2003.	2004
Change in the banking environment	2.0
Provision of services	2.4
Lending	2.0



Focus groups generally concluded that the banking environment for SMEs is changing for the better (average rating 2.1). In their opinion, the quality of services is improving and banks are putting more effort to attracting new clients. Clients, on their part, are gradually losing their mistrust in the stability of banks. On the other hand, there is great frustration because competition in the number of banks has not led to competitiveness in the cost of loans, the range of services and terms for lending to SMEs.

***“Banks have introduced e-banking, and the efficiency of services has been significantly improved.”***

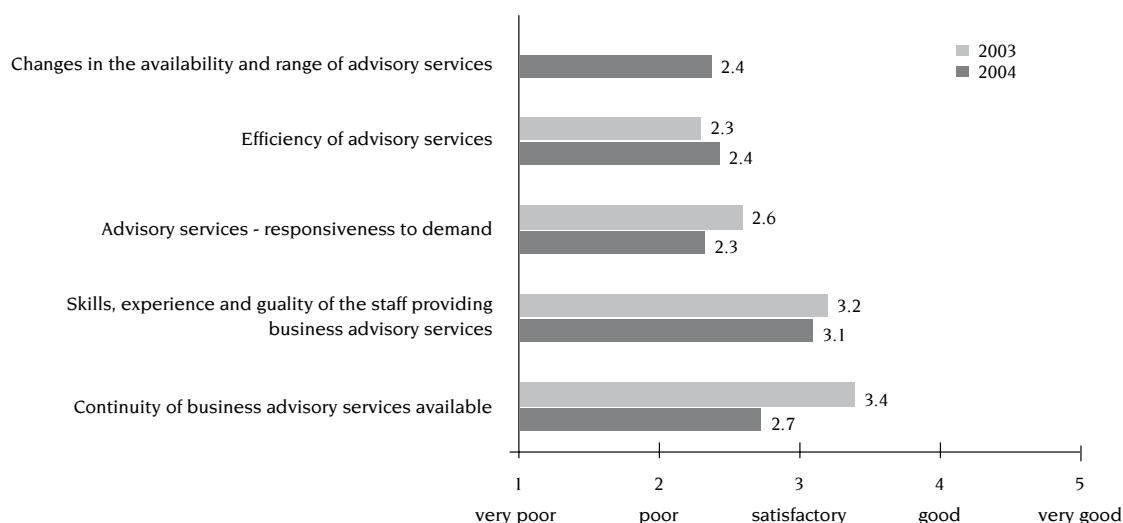
## 6. Advisory Services for New and Small Businesses

The following issues were researched under this heading:

1. Use of advisory services and satisfaction with the range and quality of advisory services available to new entrepreneurs and SMEs, rating of the services and comment on the changes needed.
2. Efficiency of advisory services operations.
3. Responsiveness of advisory services provided to the demands and the needs of enterprises.
4. The skills, experience and quality of the staff providing business advisory services.
5. The continuity of business advisory services available.
6. The change in the provision of advisory services since March 2003.

The quality of services, their availability, efficiency of advisory services and of staff providing these services is deemed “satisfactory” by focus group participants, with an average rating of 3, in line with the results from the previous study. In 2002, only the SME representatives from Montenegro gave better ratings to the quality of business advisory services in their country (OECD, October 2003, p.43).

**Figure 1.6. Average Rating for the Advisory Services Questions, 2003 and 2004.**



## Use of Professional Business Advisory Services and Their Range

25.1 Does company make use of <b>professional business advisory services</b> ?	<b>2004</b> <b>Yes: 52%</b>	<b>2003</b>
	From private consultants From government/ donor supported advisory centre	<b>Yes: 50%</b> <b>No: 85.4%</b> <b>n/a</b>

Over half of participants (52%) use business advisory services. 50% of them use services provided by private consultants, while the majority (85.4%) does not use the services provided by government/donor supported advisory centres. The most frequently used types of services are legal and book-keeping services.

***“Book-keeping agencies also advise company owners, because they know all about regulations and their changes.”***

One of the reasons for not opting for government advisory services may be illustrated by the following quotations:

***“Authorised agencies in smaller communities would fail; they wouldn't be able to cover their costs, because of insufficient demand. Companies in such communities are solving these kinds of problems in a different way.”***

***“It is done more through a circle of friends, acquaintances, people you know, who exchange opinions, views, and on that basis the decision is made on what to do next.”***

25.2 Satisfaction with the <b>range of advisory services</b> available to new entrepreneurs and SMEs?	2004	2003
Overall	<b>Yes: 38.1%</b> <b>No: 61.9%</b>	<b>n/a</b>
Services from private consultants	<b>Yes: 66.7%</b> <b>No: 33.3%</b>	<b>n/a</b>
Services from government/donor supported advisory centre	<b>Yes: 23.7%</b> <b>No: 74.3%</b>	<b>n/a</b>
Average ratings	<b>2.4</b>	<b>3.2</b>

Participants reported some positive experiences in this area, particularly with private consultants. They said they mainly use bookkeeping and legal services, consulting services for business plan creation, and some marketing services. A relatively large number of SME owners and managers (61.9%) are not satisfied with the range of advisory services available to new entrepreneurs and SMEs. The average rating of business advisory services of 2.4 came in lower than last year's (3.2). However, two-thirds of entrepreneurs (66.7%) are satisfied with business advisory services provided by private consultants, while 74.3% of participants are not satisfied with business advisory services provided by government/donor supported advisory centres. It is accepted that SMEs do need help in identifying and articulating their own needs. Even if they realise that they need advisory services, SMEs said that they find these services too expensive.

***“Private consulting companies offer services that are useful for SMEs, but they are expensive.”***

#### Efficiency of Operation of Advisory Services

26. Do advisory services <b>operate efficiently</b> ?	2004	2003
Overall	<b>2.4</b>	<b>3.2</b>
Private	<b>3.1</b>	<b>n/a</b>
Public	<b>1.8</b>	<b>n/a</b>

More than half of focus group participants (57.1%) are of the opinion that advisory services provided by private consultants operate efficiently. They assessed the work of private advisory companies as satisfactory (average rating 3.1), while the average assessment of the operation of public business advisory centres is less than “poor”, because of perceived inefficiency.

*“...Public services are inefficient....all consultations, the entire assistance you get is mainly from private consultants. Public centres are not interested in giving advice.”*

### Responsiveness of Services Provided to the Needs of Enterprises

27.1 Are services provided responding to <b>demand and the needs</b> of enterprises?	<b>2004</b>	<b>2003</b>
Private	<b>2.9</b>	<b>n/a</b>
Public	<b>1.8</b>	<b>n/a</b>

Over half of the participants (55.9%) agreed that available advisory services respond to the demand and needs of enterprises. On the other hand, there were some comments that advice given is not applicable to SMEs.

*“They sometimes advise phenomenal things, which can't be applied here.”*

27.2 Satisfaction with the <b>services provided</b> ?	<b>2004</b>	<b>2003</b>
Private	<b>2.9</b>	<b>n/a</b>
Public	<b>1.8</b>	<b>n/a</b>

The perception of the extent to which business advisory services provided from private consultants respond to the needs of enterprises is better (2.9) than those of services provided by public centres (1.8).

*“Private consultants offer what is interesting for us and what they can sell to us.”*

### Skills, Experience and Quality of Consultants

28. Rating given to the <b>staff</b> providing business advisory services received by your company.	<b>2004</b>	<b>2003</b>
Overall	<b>3.1</b>	<b>3.2</b>
Skills	<b>3.2</b>	
Experience	<b>3.1</b>	
Quality	<b>3.0</b>	

The skills of staff providing business advisory services are assessed as just above “satisfactory” (3.2).

*“It is good to hire older people, because they know the matter better. There are older experts who are excellent in following the changing regulations, they are experienced in where and how to get proper information.”*

Participants regard the experience level as “satisfactory” (average rating 3.1). They emphasised that this does not necessarily mean that the education system provides adequate knowledge, but that much is achieved through practice and experience.

***“...experience can't be obtained through diplomas and degrees, but experience is what helps us and what is significant for us.”***

The quality of staff providing business advisory services is regarded as satisfactory (3.0), although SME owners and managers in focus group discussions were concerned about the protection of their ideas and authors' rights.

***“The ethics of consultants is an issue. If you have an idea which a consultant says is good, you can be sure that you won't be the one to realise it; your idea will be stolen and realised before you even manage to register for providing consulting services.”***

#### **Continuity of Business Advisory Services Available**

	<b>2004</b>	<b>2003</b>
29. Rating given to the continuity of business advisory services available.	<b>2.7</b>	<b>3.4</b>

In discussions, participants expressed no concerns about the continuity of business advisory services available, but nevertheless the rating given was less than “satisfactory”, indicating some concerns.

#### **Change in the Provision of Business Advisory Services**

	<b>2004</b>		
	<b>Worse</b>	<b>No change</b>	<b>Better</b>
30. Rating given to the change in the provision of business advisory services for SMEs since March 2003.	<b>11.3%</b>	<b>72.7%</b>	<b>16.0%</b>

16% of participants said that positive changes have been made in the provision of business advisory services for SMEs since March 2003. However, the majority believe that there have been no changes (72.7%).

***“..book-keepers have started getting licenses, and the consultant who provides the business advisory service is responsible if something goes wrong.”***

Because of frequent changes in regulations, entrepreneurs said that it would be useful to have software containing all laws and regulations, which could provide solutions with regard to legal issues (there are several such products available on the market).

#### **7. Business Incubators**

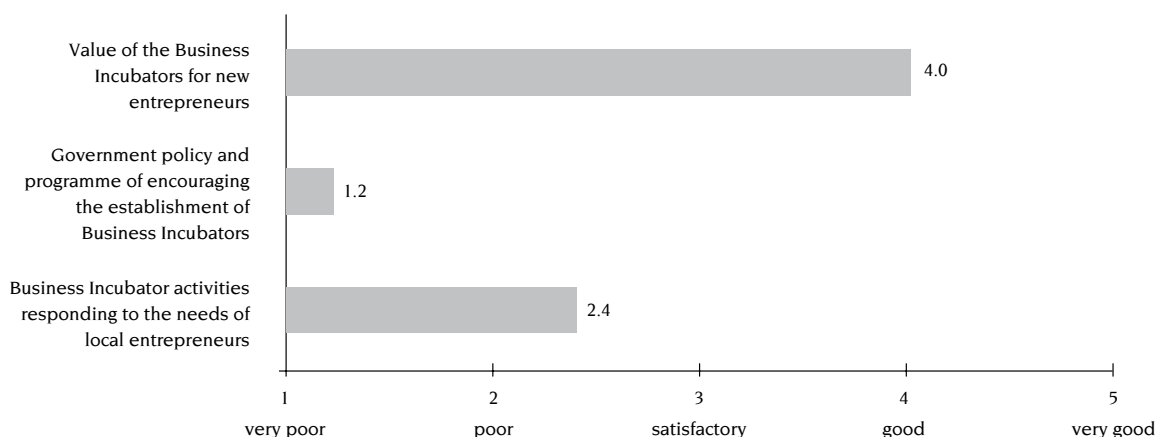
The following issues were researched under this heading:

1. Awareness of Business Incubators and the use of and the experience with business incubators; and the rating assigned to the value of Business Incubators to entrepreneurs and existing SMEs.
2. The efficiency of the government policy and programme for encouraging business incubators.
3. The response of Business Incubators to the needs of local entrepreneurs.
4. Awareness of other government/donor supported schemes for start-ups.
5. The change in government policy towards Business Incubators since March 2003.

The focus group participants could not fully answer all the questions concerning Business Incubators as there are no incubators in Serbia (except one private Business Incubator). However, when the significance

of Business Incubators for new entrepreneurs was explained to them, most focus group participants said that they believe there is a need for institutions such as these.

**Figure 1.7. Average Ratings for the Business Incubators Questions, 2004.**



### Experience with Business Incubators

	2004	2003
31.1. Are you <b>aware</b> of what Business Incubators are?	<b>Yes: 22%</b> <b>No: 78%</b>	<b>No</b>

78% of SME owners and managers who took part in discussions were unaware of Business Incubators. Following a brief explanation of the principles of Business Incubators, participants answered the questions. On the basis of the introductory explanation and dissatisfaction with the work of local administrative authorities, they gave the following answer:

***"The municipality is the biggest incubator."***

	2004	2003
31.2. <b>Use of or experience</b> with Business Incubators.	<b>Yes: 2%</b> <b>No: 98%</b>	<b>n/a</b>

Only one respondent, operating in the area of forestry, had some insight into Business Incubators. The majority of the participants (98%), had no experience with Business Incubators whatsoever.

	2004	2003
31.3. Perception of <b>importance</b> of Business Incubators for <b>new entrepreneurs and SMEs</b> .	<b>4.0</b>	<b>n/a</b>

Questions about the importance of incubators and suitability of business incubator activities for needs of local entrepreneurs were answered on a 'what if' basis. The ratings were very positive. Participants' expectations mostly concern reduction of operating costs through the use of facilities, which would not only cut costs, but also avoid problems in terms of installing and paying public utilities (electricity, sewerage, water system).

***“All of this is financial assistance in the end. They are giving you money in a way. If they gave you machines under more favourable terms, if you rented premises on more favourable terms, it means that you don't have to pay – you save money.”***

Participants said that there is a need to provide specialised support in the field of marketing. Managers of smaller companies tend to be more interested in Business Incubators and they were more inclined to recognise the potential benefits of Business Incubators. Entrepreneurs also said that Business Incubators should be encouraged in the area of food production and processing.

***“The idea of establishing Business Incubators is good; they could promote the development of SMEs.”***

There were some reservations among entrepreneurs, implying the need for precise legal regulation.

***“Who should be the owner of these incubators”***

32.1. Is the government <b>policy and programme</b> of encouraging the establishment of Business Incubators efficient?	2004  Yes: 6.5% No: 93.5%	2003  n/a
32.2. Perception of <b>efficiency</b> of government policy and programme of encouraging the establishment of Business Incubators.	1.2	n/a

Most focus group participants are of the opinion that the government policy and programme for encouraging Business Incubators is not efficient, with an average rating of “poor”.

***“There hasn't been a government policy so far, only verbal promises.”***

33. Perception of relevance of Business Incubators' activities to the <b>needs</b> of local entrepreneurs.	2004  2.4	2003  n/a
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The average rating given to the relevance of Business Incubators' activities for the needs of local entrepreneurs is between “poor” and “satisfactory”.

34. Awareness of other <b>government/donor supported schemes</b> for start-ups.	2004  Yes: 23.3% No: 76.7%	2003  n/a
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More than three-quarters of the focus group participants (76.7%) were not aware of other government/donor supported schemes for start-ups.

35. <b>Change</b> in the government policy towards Business Incubators since March 2003.	2004  No change: 85.3%
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Government policy towards Business Incubators is perceived as unchanged.

***“There has been no government policy towards Business Incubators and thus, it is the same as it used to be”***

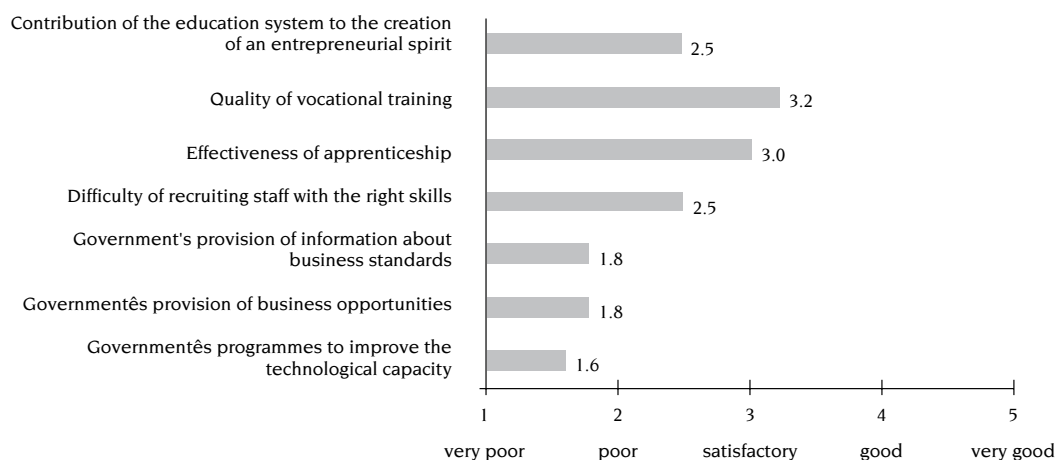
## 8. Entrepreneurship, Vocational Education and Access to Technology

The following issues were researched under this heading:

1. Contribution of the educational system to the creation of an entrepreneurial spirit.
2. Awareness of training schemes for entrepreneurs.
3. The quality of vocational training, the effectiveness of apprenticeships and difficulty in recruiting staff with the right skills.
4. Rating of government's provision of information about business standards and opportunities.
5. Rating of government's programmes to improve the technological capacity of small enterprises.
6. Rating of the change of image of entrepreneurs since March 2003.

As these questions were not asked in the 2003 report there is no comparative information and all data relates to 2004.

**Figure 1.8. Averages Rating for the Questions on Entrepreneurship, Fair Competition and Access to Technology, 2004**



### Entrepreneurship and Vocational Education

36. How much is the <b>education system</b> contributing to the creation of an entrepreneurial spirit in your country?	<b>2004</b>  <b>2.5</b>
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Answers to this question were mixed. For example, can the educational system contribute to entrepreneurial spirit development? **“Yes, it can”**. Does it actually do so? **“No, it does not”**. Participants insisted on these sorts of answers in order to accentuate the gap between the importance of education system in development of an entrepreneurial spirit in society and its actual role in doing so.

**“Our education has been the same for the last 20 years and entrepreneurship has not been a part of it. The process of creating entrepreneurship has been uncontrolled. Entrepreneurs have been learning entrepreneurial skills by themselves”.**

In addition to encouraging the development of a set of values, participants were of the opinion that it is important for people to learn the basic tools necessary for entrepreneurship through the education system, to learn foreign languages and become computer literate.

***“Pupils in secondary vocational schools do not acquire the necessary skills for independent work in companies. Because of this it is necessary to adjust the school curricula of these schools to the needs of companies.”***

37. Awareness of <b>training programmes</b> for entrepreneurs.	<b>2004</b>  <b>Yes: 46.9%</b> <b>No: 53.1%</b>
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Slightly over half of participants said they were not aware of any training programme designed for entrepreneurs, such as the National Employment Agency programmes, Chamber of Commerce training programmes and the training and seminars of the various educational institutions, consulting agencies and NGOs. Most of these programmes are not “tailor-made” for local entrepreneurs. The programmes do not address the specific problems entrepreneurs encounter in their day to day work.

38.1. Perception of <b>vocational education quality</b> .	<b>2004</b>  <b>3.2</b>
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38.2. Perception of <b>apprenticeship effectiveness</b> .	<b>2004</b>  <b>3.0</b>
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38.3. Perception of opportunities for a particular business to <b>recruit staff</b> with the right skills.	<b>2004</b>  <b>2.5</b>
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Entrepreneurs assessed the quality of vocational education for work in their companies as “satisfactory”. The main objection with regard to education of staff for particular jobs was the inadequate practical training of secondary school pupils.

***“The education system should concentrate on practical professions. Then it would be easy to train a trainee with quality knowledge for the job.”***

There is a difference between micro and medium-sized enterprises. Micro-enterprises have greater difficulty in recruiting and keeping employees. There is more demand for highly skilled staff in smaller companies.

***“I cannot afford to employ staff without experience. An employee needs to have sufficient professional experience after graduation in order to be employed in an SME.”***

Another important problem is the absence of co-operation among colleagues and help for beginners.

***“Some people are hiding their knowledge from colleagues and nobody seems to want to help the youth to learn the job.”***

39.1. The perception of government's provision of information about <b>business standards</b>	<b>2004</b>  <b>1.8</b>
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39.2. The perception of government's provision of information about <b>business opportunities</b>	<b>2004</b>  <b>1.8</b>
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Most of the information released by the government is disseminated through the various media. Entrepreneurs prefer getting information via television. The Government's website is regarded as an excellent information spot.

*"We are quite well informed, we hear everything on TV".*

*"Nothing directly. For 4 to 5 years no information has been sent addressed to this company."*

Information about business opportunities, offered by Chamber of Commerce and other organisations are sometimes perceived as a means for extorting money. The Chamber of Commerce is not regarded as being as effective as the Union of Employers.

*"... Once again someone wants to take money from us... We are receiving information through other channels... For instance, I received some important information from the Embassy of Spain."*

### Access to Technology

40. Perception of government's programmes for improvement of small enterprises technological capacity.	<b>2004</b>  <b>1.6</b>
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Entrepreneurs assessed government's programmes for improvement of small enterprises technological capacity as between "very poor" and "poor" (average rating 1.6).

41. <b>Change</b> in the image of entrepreneurs since March 2003.	2004		
	Worse 10%	No change 58%	Better 32%

Most focus group participants (58%) believed that there has been no change in the image of entrepreneurs since March 2003, while 32% believed that the image of entrepreneurs in Serbia has improved over the last year.

*"There is a little envy, even among our closest neighbours. They think you are loaded with money. Some people think entrepreneurs are criminals."*



## *Part II*

### *Chapter II*

## **ANALYSIS AND ASSESSMENT**



## 1. Institutional Framework for SME Policy

### Situation in the Institutional Framework

In addition to privatisation and FDI, SMEs and private entrepreneurs are considered to be key drivers of economic development. In January 2003, the previous Government of the Republic of Serbia adopted the Strategy for the Development of Small and Medium-sized Enterprises and Private Entrepreneurship prepared by the Ministry of the Economy and Privatisation.

In February 2004 the National Assembly of the Republic of Serbia enacted the *Law on Ministries* which defined the name and activities of the Ministry of Economy. This Ministry incorporates the operations of the previous Ministry for Economy and Privatisation. The *Ministry of the Economy* with its two departments – The Department for SME Development and the Department for Private Entrepreneurship, is responsible for defining and implementing the Strategy for the Development of Small and Medium-sized Enterprises and Private Entrepreneurship 2003-2008 in the Republic of Serbia. It is also the main state institution that:

- Defines the priorities in economic policy that impact on the private sector.
- Provides the strategic guidelines for development of Small and Medium-sized Enterprises and Private Entrepreneurship (SMEs)<sup>1</sup>.
- Coordinates and supports development of businesses and
- Undertakes activities aimed at creating a business environment for encouraging SME start-ups.

The strategy for SME development in Serbia aims to make the sector a key engine of economic development. To that end, it needs to be export-oriented and become competitive in world markets. The following are the most important social and economic objectives of the Strategy (Ministry of the Economy and Privatisation, January 2003, p. 1):

- Employment rise.
- Improvement of citizens' standards of living.
- Regional development.
- Export growth and
- Increase in the means available for other social activities.

The Strategy has two main strategic objectives for Small and Medium-sized Enterprises Entrepreneurship development over the period 2003-2008:

1. Increase the number of SMEs from 270,000 to 400,000 and
2. Create over one million new jobs.

According to the Privatisation Agency, 674 small and medium-sized companies with projected investment of €61.6 million were sold in auctions in 2003, (G17 Institute, March 2004, p. 131).

The *Agency for the Development of Small and Medium-Size Enterprises and Entrepreneurship* (ASMEE) is the chief government institution working under the Ministry for the Economy to support the establishment and development of SMEs. ASMEE is provided with funds from the Republican budget. The funds are

transferred to the Ministry of Finance, which redirects these funds to ASMEE. The Ministry of Finance said 300m dinars were allocated in 2004 for financing ASMEE, the Privatisation Agency and the Action Fund. The Ministry of Economy distributes the funds to the latter institutions. ASMEE has 100 employees, 85 of which are employed in regional agencies.

A key role of ASMEE is to deal with the problems which SMEs face in their daily work and to initiate constructive solutions. It also promotes and advocates the interests of the SME sector to the Government and other state authorities and institutions, in order to improve conditions for the start up of small businesses.

ASMEE carried out a range of activities in 2003. This included meeting of representatives of local authorities, relevant ministries, the Development Fund, the Guarantee Fund and bank associations in 13 towns in Serbia. The aim was through consultations with the SME sector representatives, to get acquainted with the problems faced by entrepreneurs and to inform entrepreneurs about the prospects for long-term development of the sector. Under the supervision of ASMEE, promotional campaigns were undertaken including a campaign "Small Business – Why Not?" and conferences on entrepreneurship were held.

As part of its publishing activities, ASMEE launched an Entrepreneurial Library. It collected and classified relevant literature (books, brochures, periodicals, papers, directories, etc.). In 2003, several publications and handbooks were published: *Business Incubators*, *How to Become an Entrepreneur*, *Methodology of Business Plan Making*, *the Legal Base of Your Business*, *Available Credit Lines*.

The transfer of know-how and technologies from the Agency's research sector to SMEs and entrepreneurs generally is carried out by providing research results, identifying entrepreneurial demand for research, laboratory research in institutes related to the needs of SME production processes and attestation of products. To carry out these activities, ASMEE has started a project on the introduction of an integrated information system aimed at providing a continuous flow of information to the SME sector. However, this information system is not yet operational because of lack of funds. Around €150,000 is required to purchase equipment and software. ASMEE is searching for a donor to provide the funds to complete the project. ASMEE keeps entrepreneurs informed in the following ways:

- SME News
- Telephone help-line
- ASMEE web-site
- Answers to entrepreneurs' questions published in daily newspapers
- Direct contact with entrepreneurs by staff particular departments of ASMEE

SMEs News is as a newsletter with 115,000 copies distributed as a supplement to the daily newspaper Politika. Up to January 2004, 7 issues had been published.

The Law on the Agency for Development of SMEs allows the Government of the Republic of Serbia to set up regional agencies for the development of SMEs. It can also organise networks of professional support to SMEs. However, in practice, the main providers of regional agencies have been local government, regional economic chambers, entrepreneurs' associations, business associations, banks, institutes, faculties and other (the Ministry of Economy, 2004, page 32).

The regional agencies, centres and offices play an important role in stimulating SME development at regional and local level with a view to increasing the number of new companies and fostering the development of the existing ones. They support SMEs in the early stages, as well as throughout their life. They provide business consulting services, training programmes and information. They also undertake projects to develop the business environment and institutional framework for the SME sector.

During the period 2001 and 2002, 10 regional agencies and centres for development of SME were set up in Kragujevac, Nis, Krusevac, Zajecar, Zrenjanin, Uzice and Belgrade. Agencies were set up with the help

of the European Agency for Reconstruction (EAR), in Novi Sad and in Subotica, with the help of the German Technical Co-operation Agency (GTZ). In Novi Pazar, the agency was founded with the financial support of the Swiss Agency for Development and Co-operation (SDC).

In 2003 and 2004, the network of regional agencies was further expanded with the establishment of four new regional agencies. These are in Sombor, Sabac, Leskovac and Vranje. The latter two were set up with the support of the United Nations Development Programme (UNDP) and the International Labour Office (ILO).

Other bodies in Serbia also play a significant role in SME development. These include: the Serbian and Yugoslav Chambers of Commerce and Industry, Regional Chambers of Commerce, the National Bank of Yugoslavia and the Development Fund of the Republic of Serbia, the Serbian Investment and Export Promotion Agency and the Serbian Export Credit Agency, established in October 2002. Last year the Agency for Rural Development was established. This is due to become operational in 2004 within the Ministry of Finance.

There are currently very few mechanisms facilitating consultation between SME stakeholders and the Government. The main such initiative is the *SME Advisory Board* (SMEAB), which includes selected business people to advise Government on priorities for reform. This has been operating since 2001 and is a potentially useful tool. It reports to the Ministry of Economy, rather than ASMEE and does not yet include the wider SME policy community. An Entrepreneurial Council was set up within the Ministry of the Economy and Privatisation as an EAR initiative and with strong support of other donors. It is composed of reputable SME owners selected by the Minister.

### **Assessment**

According to the focus group participants and the experts consulted, the institutional framework for implementation of the policy for SME development has still not reached a satisfactory level. A number of institutions have been established. The work programmes of these institutions are based on the experiences of other transition countries. Nevertheless, many of these institutions are still not operating in an effective manner, nor are their activities fully accepted by the business community. The experts consulted are of the opinion that the officials in the government's institutions are not experienced enough and are unfamiliar with the basic requirements of the SME sector.

The objectives of the Strategy for the Development of Small and Medium-sized Enterprises and Private Entrepreneurship were overestimated and are regarded as unrealistic. Its implementation is ineffective due to a lack of funds. During the period 2001-2003, there was an average of 36,326 new jobs created per year. It will take 27.5 years to employ a million people in SMEs with this employment growth rate (G17 Institute Economic Review, 40 – 41/2003, p. 3).

As highlighted in the previous EPPA report, the financial sustainability of both ASMEE and the regional network is still far from assured. ASMEE has received start-up funding, but is not guaranteed a regular state budget. The funds for most of the regional agencies are available only to assist the start-up of SMEs and not for supporting their ongoing operations. The whole network relies almost entirely on donations, leading to the possibility of problems with their continuity into the future. The regional agencies are mandated to achieve financial sustainability in a relatively short period of time (a couple of years), compared to similar bodies elsewhere in SEE.

The efforts of the ASMEE, despite its limited budget, must be acknowledged, but SME owners and managers are still not sufficiently informed about its activities. Some experts suggested that ASMEE should develop a mailing list for all SMEs and disseminate all information relevant for their work in that way, in order to ensure the information reaches everyone. This would also have the benefit of forming the basis for development of a wider database or could be tied into such a database.

Although ASMEE covers nearly 90% of the territory of Serbia, this study confirms that its activities and the other regional bodies in charge of the SME development are still insufficient to ensure achievement

of the Strategy's objectives. According to the Federal Statistical Office, in 2001 there were 41,932 active, micro, small and medium-sized enterprises. In 2002 this figure dropped to 39,120. No private medium-sized enterprises were started up in 2001 or 2002. However, 5,691 micro and small start-ups were established in 2001. This increased to 6,893 in 2002.

To improve the services to SMEs and facilitate more efficient implementation of SME support programmes, as many of the state institutions as possible should be located at a regional level. This would also facilitate consultations between the Government and local SME owners and managers and allow the small business associations better opportunities for discussions with Government representatives.

The Entrepreneurial Council has not been very successful in its work. It has adopted an overly formal approach and the then Government did not appreciate the Council sufficiently. The Council never really became operational and capable of helping to tackle the existing problems of the SME sector. It held only one meeting in February 2003.

Although the economic chambers should have an important role in supporting SME development, they do not participate enough in this process. Both SME owners and managers participating in the focus groups and the experts consulted shared the view that the Republican Chamber is much too rigid and it has undergone very little change since the fall of the Milosevic regime. SME representatives are of the opinion that the Chamber cannot represent the SME sector. On the other hand, the Union of Employers is an institution which, pursuant to the Labour Law, can represent the interests of employers. There was a general consensus that the Union of Employers should be developed further and have a special part of it dedicated to supporting SME development.

In the course of 2003, some progress was made in the implementation of the Strategy for SME Development. In co-operation with relevant ministries, ASMEE completed seven out of the eight planned operational programmes. However, the important industry operational programme has not yet been completed. The operational programmes of the Strategy (Ministry of the Economy and Privatisation, January 2003, p. 16) completed in 2003 were:

- The operational programmes for the SME sector development in the area of agro-processing, tourism and e-commerce (in co-operation with the Ministry of the Economy, Ministry of Trade, Tourism and Services, Ministry of Science and Environment Protection and the Ministry for Agriculture and Water Management, in accordance with the strategic orientation of these ministries).
- Preparation of operational programmes to support the introduction (in co-operation and in accordance with strategic orientation of ministries responsible for these areas) of:
  - a quality system
  - support for innovations in the SME sector
  - improved relations between education and science and research, and the SME sector and to
  - improve the position of SMEs in domestic market.

## **2. Rule of Law and the Regulatory Environment**

### **Situation in the Rule of Law and Regulatory Environment**

According to recent research, it is estimated that registration of an enterprise in 2003 took 40 days, *i.e.* 33 working days (G17 Institute, September 2003, p. 22). The registration of enterprises had to be done in three locations:

- The Commercial Court,
- The Republic Statistical Office and
- Centre for Credit Solvency of the National Bank of Serbia and business banks



The estimated total costs of registering a company in 2003 (G17 Institute, September 2003, p. 22) was €1,296. 27.6% of the costs of registration related to the fees for courts, statistics, banks, local government bodies and others. The costs of the services of lawyers were 43.3% and bribes cost 29.1%.

The enterprise registration procedure should be significantly simplified by the enactment in May 2004 of the *Law on Registration of Economic Entities and the Law setting up the Business Registration Agency*. Under the new law, enterprises will be registered by being entered in a central *Register of Economic Entities* at the Business Registration Agency. The Law requires the economic court to send all its documentation and electronic database information on economic entities to the Agency for Economic Registers by March 15, 2005 at the latest. This should result in a unique register of businesses where:

- Registration forms can be submitted electronically.
- There is provision for electronic connection of the Register with other registers or databases that are kept in the Republic of Serbia.
- The Business Registration Agency will issue a unique identification number for economic entities.
- All registration costs will be reduced and
- Bribery and corruption should be reduced.

Another very important law passed in May 2004 was the *Law on the National Corporation for Housing Credits Insurance*. It should encourage construction, and consequently, it should help deal with the problem many entrepreneurs have in obtaining business premises.

The *Law on Supplements and Amendments to the Public Procurement Law*, which was also passed in May 2004, set forth a simplified procedure for public procurement, lower costs and reduced scope for the abuse of procurement terms and for favouring certain bidders. The procedure for awarding a contract has been simplified and shortened, including the procedure for appeal.

The *Bankruptcy Law* and the *Law on the Agency for Licensing Trustees in Bankruptcy* were passed in July 2004. The laws will improve the protection of commercial creditors, workers and the state in collecting its due claims from the bankrupt enterprises.

The following laws have not been enacted yet, but are scheduled for adoption:

- *Company Law*, which is aimed at unifying the tax treatment of all companies.
- *The Law on Mortgages and Mortgage Institutions* which aims to deal with the problems currently encountered when taking out mortgages on property or using property as collateral for loans from financial institutions.
- Amendments and supplements to the *Law on Privatisation Agency*.
- The harmonisation of national legislation in the area of standardisation with the EU *acquis communautaire*.

The previous government undertook several steps to deal with administrative barriers including: the establishment of the Council for the Reform of State Administration. The former Ministry of Local Governance published a periodical on State Administration Reform and there was an initiative for training state administration officials.

The Government of Prime Minister Dindić established an *Inter-departmental Working Group for Deregulation*, whose basic objective was to work systematically to deregulate the economic system. The Working Group was set up as a result of pressure from international organisations, in particular of the World Bank, which funded the Secretariat in charge of preparing meetings and conducting analysis of the legal projects. The Working Group was mandated to :

- Assess all draft laws and bylaws before the Government sent them to parliament for adoption, in order to analyse the effect that these documents might have on the economy.
- Undertake regulatory impact analysis, which OECD countries conduct.

- Initiate changes in legislation and
- Work to deregulate commercial legislation.

This entailed formulating amendments to the existing laws and making recommendations on new laws that should be adopted in accordance with the market economy principle.

The previous Government also founded the *Council for Fighting Corruption* to assist in detecting and suppressing corruption. This is an independent body comprised of reputable persons from various appropriate backgrounds. This body deals with problems it observes itself and those drawn to its attention by the public. In autumn-winter 2003/2004, the Council was examining several privatisation sales.

### **Assessment**

The Central Register should improve the efficiency of the registration procedure. SME owners and managers participating in the focus groups very much welcomed the initiative of the Ministry of the Economy and Privatisation in setting up the Business Registration Agency where all necessary formalities related to registration will be carried out and a uniform centralised database will hold information.

The legal environment for SMEs in Serbia has improved as a result of the new laws that have been enacted, but the full range of required legal changes has yet to be made. Last year's enactment of the *Law on Financial Leasing* and the *Law on Planning and Construction* significantly improved the economic environment. On the other hand, the *Law on Enforcement Procedure* which was enacted in 2000 and the *Law on Financial Markets* which was passed last year fell short of expectations.

The *Law on Enforcement Procedure* does not deal with the major issue of creditor protection. Many of the focus group participants and a number of interviewed experts drew attention to the slow pace in the making and enforcing judicial rulings. They described the work of the courts as inadequate. This situation is one of the key reasons why banks and other financial institutions are not yet able to increase lending to SMEs.

The principal problems with the judicial system highlighted by the experts consulted concerned unequal application of law to all entrepreneurs. The 2003 Transition Report (EBRD, 2003, p.40) also found that the courts and other institutions in charge of enforcement procedures were very unreliable and non-functional.

The *Law on Insurance of the Collection of Claims* (of creditors and suppliers from debtors) should be enacted and appropriate amendments made to the *Law on Contracts* and the *Law on Enforcement Procedure* made.

The *Law on the Financial Market* was not immediately applied, and this brought about undesired consequences. For example, the Belgrade Stock Exchange did not operate for a couple of months, brokerage houses were not able to register in accordance to the new law. This meant that they had to work semi-legally, and there is still no sign of turnover growing on the financial markets.

The *Company Law*, the *Bankruptcy Law* and the *Law on the Agency for Licensing Trustees in Bankruptcy* laws should solve several problems when enacted:

- Avoidance of settlement of obligations toward creditors.
- Accumulation of debt in one company by a person who at the same time has shares in another company.
- Accumulation of debts in "phantom" companies.
- Tax evasion and
- Evasion of social insurance contributions.

The new Bankruptcy Law should be adopted as soon as possible. In parallel with its adoption, court practice should be improved through the education of trustees in bankruptcy and the standardisation of the bankruptcy procedures with a view to accelerating the process and preventing the present situation where it can take several years to resolve the status of a bankrupt company.

Current problems in SME financing would to also be helped to a great extent by the enactment of the *Law on Mortgages*.

The harmonisation of national legislation in the area of standardisation with *acquis communautaire*, which sets down clear procedures and with standardised costs, should be urgently progressed to

- Create the conditions for domestic entrepreneurs to adjust to global and European standards,
- Allow necessary tests and certification to be undertaken in the country and
- Acquisition of appropriate marks (certificates).

Many changes are carried out following recommendations (sometimes even under pressure) of the international community, and with a desire for the country to join the EU and the developed world. Some of the recommendations are accepted, but often key parts are not included. This results in partial solutions which are sometimes mutually incompatible, or incompatible with other legislation. Frustrated focus group participants sometimes commented that “*we used to have a better system in the past, which, although being obsolete or unjust, was at least consistent*”.

The experts consulted also highlighted the lack of coordination by different parts of state administration, especially the regulatory and controlling institutions of different ministries. While some inspectors are reasonable in the application of the rules, others require rigorous application of particular standards, with difficult procedures and much documentation, for example, in relation to construction and renovation of facilities, placing considerable burden on developers, barriers to the work and proceeding and creating opportunities for corruption. Many of the participants said that complicated procedures are only surmounted either with the help of friends and acquaintances who hold relevant positions or by bribing responsible officers.

The procedures for obtaining licenses and certificates for different activities are still too complex and not organised in a standardised way. This area suffers several problems:

- Inaccurate and outdated bylaws which sometimes contain meaningless requirements given modern technology (the most remarkable are outdated regulations governing fire protection, the ordering of motor vehicles, *etc.*).
- Products already examined and certified in other countries (*e.g.* with mark CE or EU) need to be certified again in Serbia in accordance to domestic regulations.
- Serbian exporters also have problems with the certification of their products.
- A large number of certification laboratories equipped with donors' assistance do not operate due to the ignorance of government officials and
- Lack of clarity on from which budget the costs of adaptation of laboratory premises should be funded.

Overall, administrative barriers still considerably hold back the economy. The programme for the reduction of legal/administrative barriers is effectively a dead letter according to the experts consulted. There has been little visible progress in this area.

The participants in the focus groups welcomed the establishment of the *Inter-departmental Working Group for Deregulation*. However, they said its recommendations are not mandatory and its role within the system of the Government is not clearly set down. They believe that neither the Council nor the Government seemed ready to start the necessary legislative reform. The *Inter-departmental Working Group for Deregulation* should be reinvigorated, its problems resolved and its work progressed.

### 3. Tax Policy for Small Businesses

#### Situation on Tax Policy for Smaller Businesses

As indicated in last years report the main focus of Serbian *tax policy* in recent years has been to work towards neutrality and transparency in the tax system. Lower nominal rates, for example on payroll taxes and a broadening of the tax base have yielded increased revenues (OECD, 2003, p.14). This marked a break with the past which was characterised as: “a confusing mass of taxes, tax rates, and exemptions” (OECD,

2003, p.77). Major tax reforms were undertaken in the first half of 2004. However, much activity still evades tax altogether, resulting in a higher burden on compliant companies.

The sources of revenue at the *federal level* include, sales tax and excise and customs duties. Other taxes, including personal income taxes and corporate taxes, social security contributions, surcharge taxes (for social programmes) and property tax operate at the *level of the republic*. Tax collection, regulation and compliance are also the responsibility of the republic.

*Employment income* is subject to a flat rate of 14% withholding tax. In addition to the personal income tax on salary, employers calculate and deduct three types of social security contributions, namely pension and disability insurance, health insurance and unemployment insurance (altogether about 16%). *Personal income tax* rates are progressive in nature and range from 10%-20%. It is anticipated that they will be reduced to 10% in the future.

All enterprises are subject to the *company profits tax regime*, which was 20%, but has been reduced to 14% in 2003 and is due to reduce to 10%. There is a *tax credit* of 30% against profit tax liability (up to a ceiling of 70%), for SME investment in fixed assets (except for items such as cars, furniture, carpets and paintings). The unused part of the tax credit may be carried forward over a period of five years. This is not yet widely used. Companies that employ new workers are entitled to a tax credit of 40% on gross salaries paid for the first two years.

Companies also benefit from:

- Accelerated depreciation for certain categories of fixed assets (such as IT and training equipment).
- Carry forward of losses generated from business activities.
- Tax exemptions for employment of disabled people.
- Tax credits for branches located in underdeveloped regions.

A *sales tax* is levied at a rate of 20% on goods and services (except for basic food products) and is not deductible.

The existing Government has adopted the tax laws that are focused on the reduction of tax rates and widening the base of taxpayers. With that aim, the following changes in tax legislation have been enacted:

- The Law repealing the Wages Tax Bill.
- The Law on Amendments and Supplements of the Law on Citizens Income Tax.
- The Law on Value Added Tax.
- The Law on Amendments and Supplements of the Law on Companies Profit Tax.

The tax on earnings fund has been abolished with the aim of reducing labour expenses and encouraging employment. The tax rate for the earnings fund had amounted to 3.5%. This will not have to be paid starting from July 1, 2004. The rate of tax on earning is still 14.0%. The rate of tax on citizen's income has been reduced to 10% from 2004.

Additional allowances for enterprises will be provided when the proposed *Law on Amendments and Supplements to the Law on Company Profit Tax*, is enacted under which taxable profit will be calculated in accordance with international accounting standards. The rate of tax on companies' profit will then also be reduced from 14% to 10% and will be the lowest in the region. The tax on financial transactions is also to be reduced, and from January 1, 2005 it will be abolished. The tax rate on financial transactions has been 0.22% since April 2003.

In 2003, revenues from social insurance contributions nominally increased at a slower pace compared to total nominal wages, implying lower efficiency in collection of contributions compared to a year earlier (G17 Institute Economic Review, 40 – 41/2003, p.6). However, revenue collection in the first months of 2004 has improved considerably compared to the same period last year. Total public revenue collection

in the first quarter of 2004 rose nominally by 15.7% year-to-year (G17 Institute Economic Review, 48 – 49/2004, p. 21).

## Assessment

The general assessment of focus group participants and experts is that some progress has been made in improving the tax system and tax policy to encourage SME start-ups and the development of small business in Serbia. However, the tax system is still not sufficiently stable and transparent. Procedures are too complicated and SMEs suffer a relatively large tax burden.

Changes in the fiscal system are necessary, as analyses had shown that the existing fiscal system compromises development by being detrimental to economic effectiveness (G17 Institute Economic Review, 42–43/2003, p.22).

Improved stability, simplicity and transparency in the tax system could be achieved through the introduction of value added tax. This would also reduce the number of tax instruments which make the existing tax system relatively complicated for SMEs and entrepreneurs. Moreover, the introduction of VAT would increase the efficiency of tax collection, and consequently, SMEs' profits would be subject to lower taxes.

Focus group participants stressed that tax policy has not been consistent with other government policies, in particular, for encouraging starting up new and developing the existing SMEs with a view to employment growth and companies are not treated equally in tax collection. In their opinion, socially-owned and state-owned companies are treated more favourably than private companies. They believe that if all tax payers were paying their appropriate tax and social insurance contributions the tax burden would be much lower, and there would be less declaring of lower profits than actual and tax evasion.

The tax system and tax policy must be harmonised with the national strategy for SME development and other macroeconomic policies, to create a favourable environment for investing in SME start-ups and further development of the existing SMEs.

Tax administration has to get rid of its bureaucratic approach and to start working more efficiently, especially at the local level. Training of staff employed in tax administration is essential. To ensure efficient application of the newly reformed tax system training should also be made available for the administrative staff dealing with finance and tax in SMEs. Research on the attitude of entrepreneurs to taxes (G17 Institute, September 2003, p. 117) showed satisfactory regularity in paying taxes in the course of 2003. 57% of enterprises paid profit tax regularly, and 10% of companies with only a short delay. A significant improvement was achieved in the regularity of payment of pension and health insurance contributions. 77% of enterprises paid their contributions regularly and 19% with a short delay.

Creation of an effective tax policy and system and its efficient implementation would result in a further reduction in the grey economy. Last year's recommendation about the widening of the tax base, in order to reduce the number of tax payers who evaded taxes, is once again brought forward.

To ensure fair competition, it is also recommended that tax collection activities should be applied consistently to companies of all size, in order to prevent the situation where big companies are in a more favourable position than medium, small and micro companies.

## 4. Financial Instruments for New and Small Businesses

### Situation on Financial Instruments

There are two main types of banks in the Serbian economy: foreign banks, which are fighting strongly for market position, and the traditional domestic banks, which do not appear to be as proactive. Domestic credit to the private enterprise sector remains limited at less than 10% of GDP in 2003.

There are a total of 47 banks operating in Serbia (including Jugobanka Kosovska Mitrovica A.D.), of which nine banks are in majority foreign ownership. These 47 banks employ a total of 22,290 persons. The average age of banking officers has decreased. Many of those who lost their jobs after the liquidation of the four largest banks failed to find new employment in the banking sector. Their places were filled by younger more educated recruits.

Interest rates in Serbia in 2003 have been slowly decreasing, mostly as a result of stabilised inflation. Both interest rates and inflation recorded a lower level than in 2002 (G17 Institute Economic Review, 40 – 41/2003, pp. 7 & 14), although some increase in inflation has occurred during 2004.

According to data from the NBS, in December 2003 the annual weighted lending rates of banks were 15.48% on short-term loans and 10.87% on long-term loans, while the annual inflation rate in Serbia was 11.7%. Although interest rates grew slightly in February and March 2004, interest rates are expected to go down over the medium-term (G17 Institute Economic Review, 46 – 47/2004, pp. 14 & 20).

A *Guarantee Fund* started operating in December 2003. The Fund provided automatic criteria to the banks, and delegated the right to authorise loans and issue guarantees up to certain limit, in accordance with the criteria, thus transferring all rights to the bank and simplifying the procedure. There are also some initiatives to establish local guarantee funds, but the appropriate legal framework still does not exist.

The *Development Fund of the Republic of Serbia* was founded in 1992. The assets of this fund are intended for lending to SMEs, stimulating production activities and entrepreneurship. The Fund approves loans to economic entities directly or via the commercial banks. Since March 2003 the fund has approved loans for a total of 1,193 companies (954 long-term and 239 short-term loans). The majority of loans were approved to companies in the Belgrade area, (129), Raški (118) and Zlatiborski District (99). Most of the loans were given to finance primary production (360), agro-industry (274), wood processing industry (123) and the metal processing industry (108).

Microfinance Bank have been approving credits to the SME sector since the beginning of 2004, the Nacionalna stedionica Bank has entered into this arrangement with the help of know-how received from the German bank Sparkasse. The initial experience was that the first credit lines (EUR 15 million by the end of 2003) were placed very quickly. Demand is great; some bankers estimate it at not less than €1 billion for SMEs. Experts estimate that Serbia needs about €700 million of working capital on an annual basis, and twice as much investment capital, *i.e.* about €1,500 million. Meanwhile Pro-Credit Bank has continued to provide loans to entrepreneurs and small businesses. Nearly 12,000 loans were granted in 2003.

The *Law on Leasing* was adopted in May 2003.

## Assessment

Good reform progress has been achieved in the banking sector. Most of the focus group participants and experts consulted shared this impression. There is stability, competition and a growing number of foreign banks. However, bank services to SMEs are still underdeveloped.

The professional community assesses the banking market in Serbia as being “slightly over-banked”. The 47 banks operating in Serbia are regarded as too many for a market of 7.5 million inhabitants and a GDP of around CSD 1,100 billion (around 2,500 US\$ per capita in 2003).

It is still very difficult for SMEs to obtain a loan. A lot of banks have indicated more focus on the SME sector, but the practice on the ground is quite different. Banks are slow to enter the guarantee scheme. Only 18 banks have entered into a contract to cooperate with the Guarantee Fund and only three guarantees have been issued so far. The practice of transferring all rights to the banks is still not functioning in a satisfactory manner. Banks are still cautious in approving credits to SMEs, fearing that they will not be able to repay their loans. The focus group participants said one of the reasons is that they have large non-performing

credit outstanding to the big illiquid state-owned and social-owned companies. In spite of the increasing competition, there isn't a general expectation that commercial banks will develop any special supportive attitude toward SMEs in the near future.

Foreign banks are ready to authorise loans under more favourable, European terms for good clients. The situation is quite the opposite in terms of cost, financial terms and level of services offered by the domestic banks. The credit rating procedures in domestic banks are outdated. Loan authorising procedures are lengthy and costly. Loans to SMEs are not considered on a portfolio basis, allowing that some will inevitably fail. Every one is evaluated individually because of the fear of risk inherited from the past. The perception is that in Serbia it is very difficult for a person wishing to start up a company and who has a marketable, financially and technologically viable idea to get support.

Demand for loans is many times higher than the supply. Appropriate conditions have not yet been created to facilitate mortgages. The Central Depository of Mortgages and Pledges has not been set up and the law on mortgages has not been passed. Because of very strict conditions for obtaining a mortgage (particularly in the area of property valuation), many entrepreneurs avoid mortgages.

One of the conditions for obtaining loans is to present a profit and loss account. Many companies in the past reported a lower profit in order to make some savings on taxes. This is now causing serious problems with banks that calculate the financial position of applicant companies following strict banking rules and find it difficult to authorise loans.

The *Law on Leasing* is a huge step forward in terms of easing the purchase of equipment. Unfortunately, it is currently mostly used for the purchase of cars. Focus group participants who are familiar with the opportunities of leasing were very positive about it as a means of financing. However, they also believe that there is a shortage of personnel qualified to perform these activities. The regulation of the issue of leasing must be followed by the development of new services such as factoring and information services which could be helpful for development of the SME sector.

The effect of the risk perception on the banks and interest rates is also substantial. *The Law on Enforcement Procedure* still does not guarantee the security of creditors, so Serbia and Montenegro (former FR Yugoslavia) traditionally ranks very low on the list of countries in relation to the risk of investment (Slovenia 23, the Czech Republic 35, Slovakia 37, Hungary 37, Poland 39, Bulgaria 41, FYR Macedonia 62, Croatia 42, Romania 46, and Serbia and Montenegro 71 – Economist Intelligence Unit, 2003). According to the results of the Global Competitiveness Report, Serbia has a very unfavourable credit rating. Serbia was in a 74th place of 76 countries that were rated according to this criterion (Jefferson Institute, 2003, p 223). The law governing the security of creditors and claims must be urgently introduced.

There is still a strong need to improve the expertise of bank officers. And investment in new technology by banks, which only recently commenced, needs to be accelerated.

## **5. Advisory Services for New and Small Businesses**

### **The Situation on Advisory Services**

Services, such as business consultancies, training and tax consultancies still have not not developed significantly in Serbia. International donors and organisations such as the European Commission, the Department for International Development (DFID), USAID, UN Development Programme and World Bank have only recently started to develop business information and advisory agencies, in line with their programmes elsewhere in SEE. A WB/IFC SEED programme focusses partly on raising capacity in the provision of business consulting services for SMEs.

In terms of the public sector, ASMEE opened ten regional offices in 2002 covering 60% of Serbian territory. In 2003 and 2004, the network of regional agencies was further expanded with the establishment

of four new regional agencies in Sombor, Sabac, Leskovac and Vranje. The latter two were set up with support of United Nations Development Programme (UNDP) and the International Labour Office (ILO). These regional offices deal with the education of prospective entrepreneurs through orientation training, recruiting entrepreneurs for advanced courses and finally training them to create their own business plans. The National SME Strategy anticipates the opening of more regional offices and local sub-branches. However, as the resources for the establishing and running these offices come from international donors such as EAR, GTZ and SIDA, it is unclear whether this ambitious programme can be implemented and sustained in the long term.

There are four sets of compulsory *Chambers of Commerce and Industry* which also provide advisory services at federal, republican, provincial and regional level. Within the Chamber system, there are also general associations of entrepreneurs (sole proprietors) at municipality level.

Other bodies in Serbia also play a significant role in SME development. These include: the National Bank of Yugoslavia and Development Fund of the Republic of Serbia, the Serbian Investment and Export Promotion Agency and the Serbian Export Credit Agency, established in October 2002

The Entrepreneurial service of ASMEE provides financial and legal consulting. However, the work of this service is limited by the still underdeveloped network of regional agencies/centres. In 2002 ASMEE in co-operation with the National Employment Agency organised training under the title “*How to Start a Business*” in 20 branch offices of the National Employment Agency throughout Serbia. The National Employment Agency also set up six entrepreneurial centres in Serbia to encourage the development of an entrepreneurial culture and employment. Over the last two years the programme to improve education for entrepreneurship included learning consulting skills. For example, the project “*Non-financial Support to the Development of the SME sector in Serbia*” funded by the EAR had an emphasis on the creation and strengthening of the market of training and consulting services in Serbia.

Within the project “*Development of Entrepreneurship and SME in South-eastern Europe*”, the Republican Development Bureau implemented two programmes in 2003 – one dealt with the vocational education of entrepreneurs and the other was in the form of a seminar addressing business planning, strategic planning and marketing strategy.

**Table 2.1 Number of SMEs which used services of the national and regional agencies for SME development, 2003**

Agency	Help line	Consulting (financial and legal)	Business plan (help and creation)	Education	
				No. of seminars	No. of attendants
National	5,895	3,020	486 (help)	74	2,178
Regional	15,424	4,485	177	264	3,533
<b>Total</b>	<b>21,319</b>	<b>7,505</b>	<b>663</b>	<b>338</b>	<b>5,711</b>

Source: ASMEE (Ministry of Economy, 2004, p.32).

## Assessment

Advisory services for small business are not sufficiently developed and, except for accounting and legal services, the services that are available do not fully meet the needs of enterprises.

It is very difficult to sell intellectual services in Serbia, especially to small businesses, which are price-sensitive and have very concrete needs. SME owners do not use advisory services extensively. They said this is because they are an additional financial burden in the context of the difficulty of raising finance, a lack of confidence in the integrity of the advisors and because the range of choice of services is limited.



Both experts and SME owners and managers are of the opinion that Serbian entrepreneurs do not have a culture of using professional services. The main advisory services used are those of private consultants. These tend to be used more than those of the state agencies/centres because of specific skills that they have that the public services do not have. The services from private consultants would mainly involve accounting services, helping in business plan preparation and helping with applications for loans from banks. Consultants are concentrated mainly in Belgrade and a few bigger towns in Serbia. There is also a drain of consultants from state services into foreign consulting houses, which offer better quality of services. Services provided by institutions funded from donations or state budgets can be more attractive in terms of cost to the SME, but entrepreneurs often do not know of the existence of such services, indicating that their promotion is unsatisfactory.

The ASMEE with its network of regional centres and agencies provides advisory assistance to SMEs. Achieving sustainability, delivering effective services, partly on a commercial basis, and effective co-ordination of the network of regional offices will be major challenges confronting ASMEE.

The services and programmes offered by these agencies are mainly focused on start-ups and the problems entrepreneurs face when they are starting their small business. Consequently, there is no adequate system of advisory services, either in the private or state sectors, tailored to the needs of those SMEs which have been operating for some time. Some experts expressed the opinion that advisory centres supported by government or by donors (*e.g.* EAR, ILO), are not competent enough to be involved in this kind of activity, because the staff of these centres have sometimes only attended some short training courses which is regarded as insufficient to work as a consultant.

The average rating of business advisory services of 2.4 came in lower than last year's (3.2). The quality of business consultants depends on their professional orientation. Consultants providing accounting services and those helping in business plan creation are deemed to have satisfactory skills and are available. Focus group participants reported positive experiences in this area, particularly with private consultants. They said they mainly use book-keeping and legal services, consulting services for business plan creation, and some marketing services. Two-thirds of the SME owners and managers are satisfied with business advisory services provided by private consultants and nearly 60% of focus group participants are of the opinion that advisory services provided by private consultants operate efficiently. However, three quarters of participants are not satisfied with business advisory services provided by government/donor supported advisory centres. Management consulting is still believed to be overly academic and not fully reflect the needs of SMEs.

The chambers of commerce concentrate more on the problems of big companies. For this reason, the SME sector does not consider chambers very helpful in solving their specific problems.

Unethical and unprofessional conduct by persons who present themselves as expert consultants, but who in practice are actually not appropriately qualified or experienced effects the confidence of the SMEs in the industry. Institutions providing advisory services need to be accredited. Certificates of accreditation should be issued by ASMEE. This Agency could also coordinate all development programmes, provision of literature and teaching equipment in the area of entrepreneurship.

Reliable high quality information is very important for the SME sector, for use in business projections and business plan development. Sectoral analyses and reliable data are poor or even non-existent in Serbia. There isn't even precise data on the actual numbers employed in the SME sector. SME owners and managers are of the opinion that the government and its agencies could significantly improve public information of this type and improve monitoring.

## **6. Business Incubators**

### **Situation in the Area of Business Incubators**

There are currently neither laws nor regulations for establishing business incubators in Serbia. However, the Government has recognised the potential importance of business incubators and in 2002 initiated the

drafting of a law enabling their establishment in Serbia. This included financial and tax incentives for the registration of incubators, import of equipment and employment of new personnel. The *National SMEE Strategy* also deals with the issue, tasking ASMEE with responsibility for establishing them within the broad context of encouraging innovation, as well as for facilitating the development of privately owned business incubators. Stressing that SCG is the only country in the region without a business incubator, experts from the ASMEE are of the opinion that this is the area the Serbian entrepreneurs are least aware of at the moment.

Currently, Serbia has only one private ICT incubator in Belgrade (ASMEE, April 2003, p. 33). Initiatives for the establishment of Business Incubators supported by donors have resulted in three projects that are supposed to be implemented during 2004 (ASMEE, April 2003, p. 33). One project involves establishing a pilot business incubator in the vicinity of Niš with Norwegian support; for this incubator is expected to be an example of “good practice”. The second project, supported by Sweden, is an attempt to establish a technology business incubator with the University of Novi Sad. Finally, there is a project to establish an incubator in Knjaževac, within the IMT enterprise.

### **Assessment**

Business Incubators have been planned since 2001, but there has been little progress. The limited experience that there is based on a few attempts to establish incubators, the first one of which was a private initiative, so it was a commercial venture and not implementation of state policy.

In line with last years report SME owners and managers are positive about the government's policy of encouraging Business Incubators and have a clear wish that matters be moved along more expeditiously. The idea of lowering operating costs by sharing facilities and services is very appealing for SME owners and managers. A common view is that an objective should be to create an example of good practice through a public-private sector partnership. The focus group participants and experts believe that the local authorities should take a lead in their implementation. The experts consulted said that incubators should not be limited only to new technologies.

There was a view that Business Incubator implementation requires a legal/regulatory framework to regulate the activities of Business Incubators. There was concern about their longer term role and relationship with SMEs (*e.g.* “Why would anyone give you everything for nothing?”).

Business Incubators must be tied into the real needs of local entrepreneurs in order for projected benefits to be fully realised.

## **7. Entrepreneurship, Vocational Education and Access to Technology**

### **The Situation**

The educational system has started contributing to the development of an entrepreneurial spirit. Experts said that the situation has been improving since 2002. Entrepreneurship is being introduced as a subject in some vocational secondary schools (for example, in the form of a pilot project in the final year of agro-processing schools).

Training for small entrepreneurs is organised through the network of regional agencies, and various institutions such as National Employment Agency (NEA) and the Chamber of Commerce are involved in the implementation thereof. NEA organised entrepreneurial activities within the *Active Search for Employment Programme*. The Chamber of Commerce organises various courses. Start-up programmes are also offered.

Disseminating information on business standards and business opportunities is the responsibility of bodies such as: IECC (Euro Info Correspondence Centre), Chambers of Commerce, ASMEE (national and regional level), SIEPA – Serbian Investment and Export Promotion Agency (assessed as sluggish in programme implementation). It is not known what institution is responsible for collecting, updating, translating officially

and distributing accounting standards. The Ministry for International Economic Relations deals with food-related standards, while the Ministry for the Economy and Privatisation has published a booklet containing various standards (sanitary, health, *etc*).

## Assessment

The general opinion of both entrepreneurs and experts consulted is that the educational system must be further adjusted to meet the needs of SMEs. In-house training of staff is very important for SMEs. Management training programmes should address thoroughly the issue of in-house training and socialisation of employees. Training in safety and the regulation of safety measures in SMEs is also very important.

The absence of standards and licenses causes training problems for small entrepreneurs and they regard the training market as “quite chaotic”. The entrepreneurs themselves said that it is difficult to opt for particular training as they do not know how to assess and compare what is offered on the market.

Since 2003, the quality of vocational secondary education has been improving through Vocational and Educational Training (VET) programmes. Good VET programmes are also offered in banks. There is a need to introduce a two-year education programme for crafts.

Small enterprises need changes to the education curricula to reflect their needs. The efficiency of the apprenticeship and practical training programmes is problematic from the point of view of SMEs because they are not fully aware of the range of programmes available and if they know about them they believe their requirements are not precisely taken into account and consequently the training programmes do not match their needs. Over half of the focus group participants (53.1%) said they are not aware of any training programme designed for entrepreneurs, such as the National Employment Agency programmes, Chamber of Commerce training programmes, and the training and seminars of the various educational institutions, consulting agencies and NGOs.

Experts consulted believed that SME managers and owners do not systematically review their own businesses educational and training needs.

Government programmes for advancing the technological capacities of small enterprises are not being implemented because of the lack of budgetary resources. (*“The programmes just aren't active.”*).

SME owners and managers first have problems recruiting staff possessing required professional skills and experience, and when they finally recruit such workers and help them develop their expertise, they have problems keeping them.

The situation in the labour market is further complicated by the increasing presence of illegal workers from Romania, Bulgaria and China. Serbian experts, especially in the area of IT, tend to work for foreign companies.

Although entrepreneurs and owners of SMEs comprise a very heterogeneous group it must be stated that as a group they “deserve” a better image. Negative stereotyping in the media is in contrast to their actual contribution as employers and tax payers. It is vitally important to communicate the positive message that entrepreneurs are the people who employ other people, who pay taxes and who contribute to society generally.

## Note:

1. The abbreviation SMEE is an expression used for small and medium-sized enterprises and entrepreneurship. The strategy for Development of Small and Medium Sized Enterprises and Private Entrepreneurship produced by the Ministry for Economy and Privatisation covers development of SMEs and private entrepreneurship (this includes private craft shops that on average have around two employees including the shops' owners). Private craft shops have existed in Serbia for several decades. Their activities mostly consisted of crafts, but since 1989, their activities have spread to other activities, especially services. This research included only owners and managers of small and medium-sized private enterprises. But, the strategy includes private entrepreneurship (in craft shops), so in that context in certain places in the report, particularly when referring to the potential clients of ASMEE, the term SMEE is used.

## 8 Report on the implementation of the 2003 EPPA Policy Recommendations

In this section we assess progress in implementing the 2003 EPPA recommendations.

<b>EPPA 2003 Recommendations on Institutional Framework</b>	<b>Progress since EPPA 2003</b>
<i>Financial stability for ASMEE and the Regional Network</i>	
1. Secure and stabilise the medium term future of these organisations through a mixture of national and international resources.	<b>Limited Progress</b>
2. Ensure adequate financial support for the effective implementation of the National Strategy for the Development of SMEs and Entrepreneurship (2003-2008).	<b>Limited Progress</b>
<i>Inter Ministerial Co-ordination</i>	
3. Implement an Inter-Ministerial Group on SME Policy, co-ordinated by the Ministry of Economy and including key Ministries such as Ministry of Finance.	<b>No Progress</b>
<i>SME data and analysis</i>	
4. Co-operate with the statistical office and relevant Ministries in order to systematically collect statistical information and address the notable data gap on SMEs in Serbia.	<b>Limited Progress</b>
5. Monitor the implementation of the National SME Strategy on a regular basis	<b>Limited Progress</b>
<i>Communication with SME Stakeholders</i>	
6. Communicate and consult with SMEs on Government policies and strategies by developing more representative, regular and permanent mechanisms for dialogue.	<b>No Progress</b>
7. Strengthen the SME Advisory Board (SMEAB) to enable it to become a regular forum of communication and consultation with a wider range of SME stakeholders. Adequate resources are needed to make it an effective Government-SME stakeholder forum.	<b>No Progress</b>
8. Facilitate ASMEE's mandate to work closely with the organisations active in the SME field and to coordinate national efforts to develop SMEs.	<b>Limited Progress</b>

EPPA 2003 Recommendations on Institutional Framework	Progress since EPPA 2003
<i>Registration, De-registration, Re-registration</i>	
9. Implement an electronic firm registration system in the Courts covering the whole country.	<b>Limited Progress</b>
10. Introduce a single code number for each enterprise, in order to save time and costs to entrepreneurs submitting the same basic information to different bodies.	<b>Significant Progress</b>
11. Evaluate, simplify and publish the regulatory regimes that affect the setting-up phase of businesses as well as the procedures for re-registering and terminating enterprises.	<b>Limited Progress</b>
12. Move to a “One-Stop-Shop” system throughout the country (see OECD-EBRD, 2002).	<b>Limited Progress</b>
<i>Regulations</i>	
13. Develop and disseminate a check list of improvements that can be made to further eliminate, reduce or standardise the complexity of procedures for SMEs obtaining licenses, permits and certificates and set predetermined and short time duration for each procedure.	<b>No Progress</b>
14. Progress the reforms proposed by the Inter-Ministerial Working Group on Deregulation (ensure adequate resources for the Working Group) in close co-operation with ASMEE. SME stakeholders should be consulted before proposals are converted into law.	<b>Limited Progress</b>
16. Take steps to ensure a “proactive” and “enabling” approach by introducing the principle of “silent consent” (“silent consent” is where if the relevant public body fails to answer within a prescribed period, it will be deemed that consent has been given).	<b>No Progress</b>

<b>EPPA 2003 Recommendations on Institutional Framework</b>	<b>Progress since EPPA 2003</b>
<i>Policy Principles</i>	
The Ministries of Finance and Economy, in co-operation with the ASMEE and SMEAB, should work together to ensure that:	
17. Simplicity, stability and clarity are achieved in tax policy.	<b>Limited Progress</b>
18. The fiscal administration is made much more sensitive to the needs of the SME sector.	<b>No Progress</b>
19. Tax laws and regulations are consistently and fairly enforced.	<b>No Progress</b>
20. The process of amalgamation of taxes is continued.	<b>Limited Progress</b>
21. Consultation with SMEs or their nominated representatives on tax issues is carried out regularly.	<b>No Progress</b>
22. SMEs are able to obtain regular, simple and up-to-date information explaining the tax system.	<b>No Progress</b>
<i>VAT</i>	
23. Introduce VAT as soon as practicable (originally planned for 1 January 2004).	<b>Limited Progress</b>
24. Design the VAT refund period to facilitate cash flow, using the international standard of one month.	<b>Limited Progress</b>
<i>Grey Economy</i>	
25. Widen the tax base as an important means of fighting tax evasion.	<b>Limited Progress</b>
26. Strengthen efforts to collect arrears, regardless of firm size.	<b>Limited Progress</b>

EPPA 2003 Recommendations on Institutional Framework	Progress since EPPA 2003
<i>Bank-lending</i>	
27. The National Bank (NBS) should reduce the 50% minimum reserve requirement for foreign currency denominated (forex) bank deposits.	<b>Limited Progress</b>
28. Improve access of banks to commercially-costed medium-term finance for onlending	<b>No Progress</b>
29. Improve ability of banks to assess medium-term risk. Measures that would help meet these objectives include allowing banks to lend in foreign currency and creating a credit information bureau, possibly under the auspices of the NBS initially.	<b>Limited Progress</b>
<i>Non-bank lending</i>	
30. The Central Bank should allow non-depository credit organisations dedicated to lending to micro enterprises and start-ups to be set-up (it does not currently allow any lending to enterprises except through banks, thereby dramatically limiting the credit available at the bottom end of the market and to startups).	<b>Limited Progress</b>
31. Allow non-bank institutions to provide finance to micro enterprises and start-ups.	<b>Significant Progress</b>
<i>Legal reform</i>	
32. Pass the secured transactions law (due April/May 03), implement the registry for movable and intangible collateral, complete and approve the leasing law and implement a registry for leases, which must be closely linked to or part of, the collateral registry.	<b>Limited Progress</b>
33. Improve the regulatory conditions for leasing and taxation of leasing.	<b>Significant Progress</b>

<b>EPPA 2003 Recommendations on Institutional Framework</b>	<b>Progress since EPPA 2003</b>
<i>ASMEE and Network</i>	
34. National policy to continue prioritising provision of support to SMEs, especially start-ups, through subsidised business support services in order to deal with market failure.	<b>Limited Progress</b>
35. Work towards achieving financial sustainability for advisory services as soon as possible.	<b>No Progress</b>
36. ASMEE should formally review its regional network by the end of 2003 to assess sustainability and decide how the range of services should provide best value to SMEs.	<b>Limited Progress</b>
37. Strengthen capacity to support SMEs by providing resources to train existing staff and hire qualified expertise.	<b>Limited Progress</b>
38. Make national and donor financial support to business centres and regional development offices subject to the quantity and quality of the services provided to SMEs. A programme evaluation scheme should be established to provide the necessary feedback.	<b>No Progress</b>
<i>Quality and Accreditation</i>	
39. Introduce a system of certification and accreditation of business advisory bodies in order to set standards and improve confidence in the quality of the services.	<b>No Progress</b>
40. Develop and publish a customer charter in each ASMEE regional office, setting out the range of services provided and the standards that will be adhered to.	<b>No Progress</b>
<i>Representative Bodies</i>	
41. Evaluate the role of the Chamber of Commerce (membership, organisational structure, linkage with Government institutions, information dissemination at branch level), etc.	<b>No Progress</b>
42. Promote the role of business incubators to Serbian entrepreneurs.	<b>Limited Progress</b>
43. Lift the prohibition on academic staff working in organisations such as business incubators.	<b>Limited Progress</b>



## Annex I

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## *Annex II*

### **WEB SITES**

Chamber of Commerce of the Republic of Serbia: <http://www.pks.co.yu>

Regional Chambers of Commerce of Belgrade: <http://www.kombeg.org.yu>

Chambers of Commerce of Vojvodina: <http://www.pkv.co.yu>

Regional Chambers of Commerce of Kragujevac: <http://www.kg-cci.co.yu>

Regional Chambers of Commerce of Nis: <http://www.rpknis.co.yu>

Union of Employers of Serbia and Montenegro: <http://www.unija.org.yu>

Union of Employers of Serbia: <http://www.unija.org.yu>

Association of Independent Unions of Serbia – Headquarters: <http://www.sindikato.org.yu>

United industrial Union «Nezavisnost»: <http://www.nezavisnost.org.yu>

Ministry of Foreign Affairs of Serbia and Montenegro: <http://www.mfa.gov.yu>

Government of Serbia: <http://www.srbija.sr.gov.yu>

Ministry of Economy: <http://www.mpriv.sr.gov.yu>

Ministry of Finance: <http://www.mfin.sr.gov.yu>

Ministry of Labour, Employment and Social Policy: <http://www.minrzs.sr.gov.yu>

Ministry of International Economic Relations: <http://www.mier.sr.gov.yu>

Ministry of Science and Protection of the Environment: <http://www.mntr.sr.gov.yu>

Ministry of Mining and Energy: <http://www.mem.sr.gov.yu>

Ministry for Capital Investment: <http://www.mugrs.sr.gov.yu>

Ministry of Trade, Tourism and Services: <http://www.minttu.sr.gov.yu>

National Bank of Serbia: <http://www.nbs.yu>

Agency for Development of SME and Entrepreneurship: <http://www.sme.sr.gov.yu>

Privatisation Agency: <http://www.pa-serbia.co.yu>

National Employment Service: <http://www.rztr.org.yu>

SIEPA - Serbian Investment and Export Promotion Agency: <http://www.siepa.sr.gov.yu>  
<http://www.siepa.sr.gov.yu>

Stability Pact for South Eastern Europe: <http://www.stabilitypact.org>

SCEPP - Policy and Legal Advice Centre: <http://www.plac-yu.org>

Federal Statistical Office: <http://www.szs.sv.gov.yu>

Statistical Office of the Republic of Serbia: <http://www.statserb.sr.gov.yu>

### Annex III

## METHODOLOGY

### EPPA Methodology

The EPPA 2004 Research covered private micro, small and medium-sized enterprises. Since domestic legislation (*i.e.* Accounting and Auditing Law, Official Gazette of FRY, 71/2002) does not define the size of enterprises, the enterprises were classified, in accordance with the EU definition, into three categories, covering the number of employees, total annual turnover and annual balance sheet total. The EU definition is taken from the *Official Journal of the European Union*. ([http://europa.eu.int/eur-lex/pri/en/oj/dat/2003/l\\_124/l\\_1242\\_0030520en00360041.pdf](http://europa.eu.int/eur-lex/pri/en/oj/dat/2003/l_124/l_1242_0030520en00360041.pdf)).

Serbia does not have a comprehensive register of economic entities which provides all information about companies at one source. It was necessary to combine two databases. The two databases which were used in selecting entities into the sample of 50 enterprises in accordance with the above-mentioned criteria defining the size of enterprise were the “*Register of Classification Units*” of the Republican Statistical Bureau (RSB) and the *Serbian Chamber of Commerce* database on enterprises (<http://www.pks.co.yu/pks>). Data on the number of employees and total turnover was taken from annual financial statements for the year 2002, while information on the date of the beginning of business operation was obtained from the “*Register of Classification Units*”, on the basis of the founding date of the enterprises in question.

After having contacted selected enterprises (scheduling participation in focus groups by telephone), it was realised that there was some inaccuracy in the existing databases resulting from the mortality and quality / currency of data on the enterprises (in particular of micro enterprises). Some of them were entered into the register, but had never actually started operating, some had a change in the type of business, some a change of address of the registered office, and others a change of owner. Legislation provides for the possibility of concurrent registration in several lines of business, and for this reason in a number of cases, due to the change in the line of business, some enterprises could not be included in the sample.

The methodology of sampling is based on a stratified sample. Multidimensional stratification of enterprises was applied. The first level of stratification concerns the line of business. The sample of 50 private enterprises included enterprises operating in the manufacturing (34%), trade (26%), construction (12%), services (8%) and other economic activities (20%), excluding primary agricultural production. The representation of enterprises in the sample corresponds to the share of these activities in the value of the GDP.

The second stratification criterion was by the size of enterprises. Of the sample 50 private enterprises, 50% were of micro, 34% of small and 16% of medium-sized enterprises. There are no precise records on the number of small and medium-sized enterprises in Serbia. However, according to the available data, micro and small enterprises constitute about 88% of the total number of SMEs.

The third stratification criterion was a combination of territorial location of enterprises and whether they are located in developed regions. In that respect, 28% of enterprises were sampled from the city of Belgrade, 26% from Vojvodina, 28% from Central Serbia and 18% from South Serbia (excluding developed municipalities).

Finally, enterprises were classified according to the year in which they were founded. The sample consisted of 12% start-ups (*i.e.* enterprises established on or after 2002) and 88% old enterprises. Such classification of enterprises into start-ups and old enterprises conforms to the pattern of start-ups over the last two years. The sample did not include medium start-ups since there were no enterprises of that size established in the last two years.

Since this is a quite small sample, which has to be representative on the one hand, but include a sufficient number of enterprises from each stratum on the other, the allocation by strata was done by combining proportional allocation and satisfying minimum quotas by strata. The criterion for proportional allocation was the total turnover realised by enterprises by strata. The selection of enterprises was based on sampling with proportional probabilities of selection without repetition. Thus, within each stratum enterprises were selected with probability proportional to the total turnover. Lahiri's cumulative method of selection of units into the sample was applied.

A total of six focus groups were organised for March 2004, with on average eight participants in each group. Two focus groups were held in Belgrade (capital), one in Novi Sad and one in Kraljevo (economically developed regions according to the GDP per capita representing Vojvodina and Central Serbia) while two focus groups were held in South Serbia, *i.e.* in towns Leskovac and Nis, as a less developed region.

Standard templates were used for the discussion and the collection of ratings. Comparisons are made with ratings derived from focus group discussions carried out for the 2003 EPPA. The 2003 ratings are reported as background information and to provide an indication of the direction of change in perceptions. In addition to attending the Focus Groups each participant completed a detailed questionnaire which was subsequently used to provide the statistical data presented in this report.

After the focus groups, in April 2004 interviews were held with 12 experts from different sectors, including professors from the Faculty of Economics, representatives of the donor countries, EBRD, representatives of ASMEE, the Government of the Republic of Serbia from the Ministry of Finance and the Ministry of the Economy, the Chamber of Commerce, the Union of Employers, representatives of the NGO sector and consultants. The interviews were used to complete a detailed questionnaire which was also subsequently used to provide statistical data presented for the report.

The analysis in this report is based on the methodologies described above and is complemented by European Commission and EBRD assessment. All information has been analysed by the consultants engaged within Serbia (G17 Institute), OECD, EC and EBRD, resulting in the assessment presented in this EPPA.

**NOTE:** The notation SMEs and small enterprises in this report also includes micro-enterprises, which according to the EU definition ([http://europa.eu.int/comm/enterprise/enterprise\\_policy/sme\\_definition/index\\_en.htm](http://europa.eu.int/comm/enterprise/enterprise_policy/sme_definition/index_en.htm)) are independent enterprises with up to 9 employees and whose turnover or balance sheet asset value are  $\leq$  € 2 million. Small enterprises are likewise defined as having between 10 and 49 employees and turnover or balance sheet asset value of  $\leq$  € 10 million and medium-sized companies as having between 50 and 250 employees and turnover of  $\leq$  € 50 million or balance sheet asset value of  $\leq$  € 43 million.

## Annex IV

### Attainment of the EU Charter for Small Enterprise 2003 Targets<sup>2</sup>

#### Field of the Charter: I – Education and training for entrepreneurship

**Objective:** Establishing entrepreneurship as an experimental subject in Serbian secondary schools. Make it compulsory in the 3<sup>rd</sup> or final year of 2004/2005 within secondary education in agro-processing. Run two additional extra-curricular programmes of the JA/YE (Junior Achievement/Young Enterprise) programme in the 2003/2004 school year.

**EPPA Comments:** In accordance with the Strategy for Development of SMEs, the Ministry of Education and Sport has undertaken certain activities, which aim to align the educational system with the SMEs goals. The Ministry of Education and Sports and the Republic Agency for Development of SMEs formed an expert team whose task is to prepare for the introduction of the subject Entrepreneurship in secondary vocational schools, starting from September 2004. In the 2003/2004 school year, two extracurricular programmes for developing entrepreneurial abilities for secondary school students continued: *Business Innovation Programmes* (BIP) and *Junior Achievement Young Enterprise* (JA/YE).

BIP included 9 schools from Belgrade and Kragujevac, with over 200 students working with 19 trained teachers that completed (passed) the necessary training in November 2003. 30 student enterprises were formed. The teams presented their projects at the first Fair of Young Enterprise in April 2004.

In the second half of 2003, two external programmes of the organisation *Junior Achievement in Serbia* (JAS) were implemented: (1) The applied economy in which the programme *Management and Economics Simulation Exercises* (MESE) is also included; (2) the Company Programme, to develop student entrepreneurial organisations.

All preparatory activities have been completed and *Entrepreneurship* will be taught as an experimental subject to a total of 64 classes per annum within vocational education courses of three and four years duration. During the school year of 2004/2005 Entrepreneurship will be taught in the final grade of secondary schools with courses in the field of food agricultural production and processing.

**Field of the Charter: 2 - Cheaper and Faster Start-Up****Objective:**

1. Reform business registration regulations, concentrating registration formalities in an independent Business Registration Agency, which will complete registration formalities within 5 days. The relevant law to be passed in spring 2004.
2. Introduction of on-line registration (September 2004).

**EPPA Comments:** In May 2004, the *Law on Registration of Economic Entities* and the *Law setting up the Business Registration Agency* were adopted. Only after the enforcement of these laws, can it be expected that the enterprises registration period will be shortened. According to the data of the Ministry for Economy and Privatisation, in 2003, 22 days were necessary for enterprise registration, under optimal conditions, and the average is 40 days. For registering a private shop, the time period was much shorter and amounted to 3 to 7 days. Online registration is not possible at the moment. Introducing that option depends on adoption of laws on e-business.

**Field of the Charter: 3 – Better legislation and regulation****Objective:**

1. New bankruptcy law.
2. Finalising legislative procedure on other relevant laws – in particular the company law, and the e-signature law as well as the registration law mentioned in field 2.
3. The Council of Regulatory Reform will assume a proactive role to ensure a systematic inclusion of the Serbian business community in the policy and law-making process.

**EPPA Comments:** In May, June and July 2004, the following laws were adopted: The Bankruptcy Law, the Law on the Agency for Licensing Trustees in Bankruptcy, the Law on Business Registration and the Law to set up the Business Registration Agency. A draft Law on Electronic Signatures is under consideration. A Draft Law on Trade Entities (new Law on Enterprises) is undergoing consultation with all interested parties.

The Government of the Republic of Serbia established the Council for Regulatory Reform of the Economic System in order to provide support to the development of the private sector. The Council monitors the work and development of the economic sector, provides initiatives and proposals for changes in existing and new laws and gives prior opinions on the parts of draft laws relating to issues of importance for the development of SMEs (legal entities) and entrepreneurship. The basic shortcomings of the Council for Regulatory Reform of Economic System concern the official character of the decisions it makes, as well as the fact that no ministry is obliged to submit proposed regulations, which can affect the functioning of the economic system to it for consideration.



#### Field of the Charter: 4 – Availability of skills

**Objective:** Ensure that training institutions, complemented by in-house training schemes, deliver an adequate supply of skills adapted to the needs of small business, and provide lifetime training and consultancy.

**EPPA Comments:** Within the project “*Non-financial Support to SMEs in Serbia*”, funded by EU and managed by the European Agency for Reconstruction, a *Service Support Scheme* (SSS) was implemented in the period 2003/2004. One of the key tasks of the project “*Non-financial Support to SMEs in Serbia*” is to provide assistance to regional agencies for the creation of local networks of trainers and consultants for the SME sector. The Project has helped all regional agencies/centres as well as their sub-offices to identify (based on defined criteria), train service providers who could with their knowledge and experience in certain fields (legal aspects, marketing, finance, business plan, management), contribute to more efficient operations within the SME sector at local level. The number of identified trainers and consultants increased from 197 in March 2003 to 315 in March 2004.

In 2004, EBRD launched the TAM *programme*, which is financially supported by the EU, and operated through the European Agency for Reconstruction in Serbia. The main objective of the project is restructuring of potentially competitive enterprises and the development of the skills and knowledge for management through the transfer of relevant knowledge and experience from developed market economies. A special value of the programme is practical and direct contact with managers from the EU.

European Training Foundation, ISTUD Instituto Studi Direzionali with local support from SEED launched the *Project of strengthening partnership among institutions for education of managers and enterprises through the application of ETF tools* in May 2004. The Project mission is developing the capacities of educational organisations so that they can, together with enterprise’s management and using ETF tools, efficiently establish the educational needs of an enterprise, define priorities and prepare and operate training programmes.

The Centre for Professional and Vocational Education in the Chamber of Commerce of Serbia organises a series of expert seminars to raise the level of knowledge and skills of managers in SMEs. These seminars have as topics: management, marketing, electronic business, accounting and the analysis of financial reports, legal and financial aspects of establishing an enterprise, *etc.*

#### Field of the Charter: 5 – Improving on-line access

**Objective:** Encourage public authorities to increase their electronic communication with the small business sector, permitting companies to receive advice, make applications, file tax returns or obtain simple information on-line.

**EPPA Comments:** The Government, Parliament and all ministries, as well as agencies, already have web-site presentations on which information on the scope of their work is available. The National Bank of Serbia – Solvency Centre, has the Data Registry and the Registry of Accounting Reports of Legal Entities. It possesses extremely comprehensive and high quality databases of original and derived financial data. The data can be obtained via the Internet, with direct access to the Registry of Data on Solvency. Internet sites of the Republic and regional agencies for SME development are useful sources of information for SMEs regarding the overall economic environment, the regulatory framework for business operations, available sources of finance, as well as services which these institutions provide (training programmes, consulting, advice, *etc.*). EICC also enables SMEs to access a considerable number of its services via the Internet. The possibilities for on-line communication by small enterprises with public institutions are very limited, and are confined to receiving information from web sites, with an option of making inquiries via e-email.

## Field of the Charter: 6 – Getting more out of the Single Market

### Objective:

1. Pursue reforms aimed at the completion in the EU of a true internal market, which is user-friendly for small business in critical areas for development of small businesses, including electronic commerce, telecommunications, utilities, public procurement and cross-border payment systems.
2. Apply European and national competition rules to make sure that small businesses have every chance to enter new markets and compete on fair terms.

**EPPA Comments:** The *Agency for Foreign Investments and Export Promotion* – SIEPA, is involved in attracting foreign investments and export promotion for local enterprises. In September 2003, SIEPA launched the *Programme of Export Development of the Republic of Serbia*. This two-year programme is operated with financial support from the EU through the European Agency for Reconstruction, and has four components directly aimed to exporters as follows: SEMDAS – *Serbian Export Marketing Development Assistance Scheme*; SIBLAS – *Serbian International Business Linkages Assistance Scheme*; *Special training in the field of export marketing*; *Establishment of a Trade Information Centre, as a web portal containing the most relevant information of interest to exporters and potential exporters*.

*Serbian Enterprise Development Project* - SEDP funded by USAID is focused on improving the competitiveness of Serbian enterprises in the global market. The project started on July 1, 2003 and is planned to last until June 30, 2004.

EICC *Belgrade*, as a part of the network of Euro Info Centres, with its three relay centres in Novi Sad, Nis and Zrenjanin, has worked over the last year on improving the performance of SMEs on local and international markets.

The *Project Development of Entrepreneurship and SMEs on the territory of South Eastern Europe*, which is operated under the auspices of the Stability Pact for South Eastern Europe, has a specific system of incentives for the development of SMEs and entrepreneurship on the territory of South Eastern Europe.

GTN – *Global Trade & Technology Network* is one more electronic network, which helps small and medium-sized enterprises to develop trade connections, to recognise the possibilities for investments and to gain access to new technologies. GTN is available to enterprises in all branches of economic activity in 39 countries of Africa, Asia, Europe, Euro-Asia, Latin America, Caribbean and USA.

## Field of the Charter: 7 – Taxation and financial matters

### Objective:

1. Adapt tax systems to reward success, encourage start-ups, favour small business expansion and job creation, and facilitate the creation of and succession in small enterprises. Apply best practice to taxation and to personal performance incentives.
2. Improve the relationship between the banking system and small enterprises by creating appropriate access conditions to credit and to venture capital.
3. Improve access to the Structural Funds.

**EPPA Comments:** During 2003, new regimes of tax incentives were introduced. For small enterprises, the main tax incentive is exemption from taxation for investments in fixed assets, which exceed CSD 6 million, on condition that five new employees are hired and that the activity is performed in a field of special interest to the Republic of Serbia.

In June 2004, Corporate Income Tax was reduced from 14% to 10%, so that Serbia today has the lowest tax on corporate income in the Region and in Europe. Investment tax credit was increased to 20%, with maximal reduction by up to 50% of calculated tax. The tax credit for newly employed employees for a period of two years was increased and now amounts to 100% of the employment expenses for those employees. The wage bill tax (3.5%) was revoked. The new *Law on Social Insurance Contributions* when enforced will provide a reduction in the burden of employment costs on enterprises.

In the second half of July 2004, the Law on Value Added Tax, to be implemented in January 2005, was adopted. Preparations and training of the tax administration officials for implementing this law are in progress.

To provide financing for SME sector, activities are aimed at: creating a favourable environment and changes in the regulatory environment; building financial institutions and securing financial means. To improve the business environment, the Law on Guarantee Fund, the Law on Financial Leasing, and the Law on Pledge on Movables were adopted last year.

The *Guarantee Fund* has been established. This has created a more favourable environment for financing SMEs. CSD 1.5 billion for the operations of Guarantee Fund have been provided for 2004. The total amount of guarantees and super guarantees issued by the Fund is limited to 2.5 times as a maximum of the amount of fund capital.

Changes in the regulations of the *National Bank of Serbia* have created the preconditions for supporting banks and other financial organisations lending to the SME sector under more favourable conditions, as well as reductions in credit costs. The provisions of regulations of the NBS have simplified the methodology, reduced the necessary documentation and accelerated procedures for assessment of credit applications. These changes also affect entrepreneurs (sole traders), facilitating this sector in approaching commercial banks for loans.

With the assistance from international financial institutions: *The European Agency for Reconstruction*; the *European Fund for Serbia* with the support from KfW, the *European Agency for Reconstruction* and Swiss government special credit lines are disbursed for SMEs: Crediting micro and small enterprises is achieved through the specialised *ProCredit bank* and NGO *Opportunity International*, which with the support of USAID established a savings bank that provides micro credits for entrepreneurs and micro enterprises.

The Government of the Republic of Serbia also disburses financial support in the form of favourable credits for the development of the SME sector through the *Fund for Development of the Republic of Serbia*.

## Field of the Charter: 8 – Strengthen the technological capacity of small enterprises

### Objective:

1. Strengthen programmes aimed at promoting technology dissemination towards small enterprises as well as the capacity of small business to identify, select and adapt technologies.
2. Foster technology co-operation and sharing among different company sizes and particularly between European small enterprises, develop more effective research programmes focussed on the commercial application of knowledge and technology, and develop and adapt quality and certification systems to small enterprises.
3. Support actions at national and regional levels aimed at developing inter-firm clusters and networks, enhance pan-European co-operation between small enterprises using information technologies, spread best practice via co-operative agreements, and support co-operation between small enterprises in order to improve their capabilities to enter pan-European markets and to extend their activities in third country markets.

**EPPA Comments:** ASMEE has initiated actions for linking the SME sector with the scientific and research system: An *electronic stock exchange* of supply and demand for the results of scientific and research work has been launched; with the financial assistance of the EU, the pilot project *Innovative Vouchers* was initiated in order to increase the competitiveness of small and medium-sized enterprises through strengthening links between development and research organisations and SMEs; Two international workshops (with EU assistance) were organised - *Innovations and competitiveness of SMEs in Serbia* and *Innovations and Technologies for SMEs*, with some 160 participants from the public, research and SME sectors; The handbook *Business Incubators* was published; A methodology for scanning innovation capacities in our country has been developed.

Within the project *Serbian Competitiveness and Economic Efficiency*, funded by USAID, 3 clusters have been formed, through which the project works on increasing competitiveness and promotion of export: *Fruit and fruit juices producers cluster*; *Furniture cluster* and *a Textile cluster*.

During 2003, EICC Belgrade organised seminars on the application of JUS ISO 9000:2001 standard in the field of services, protection of intellectual property and patents, SE mark, EU directives and standards, approaches to harmonisation with standards from the ISO 9000 and ISO 14000 series; moreover, two information seminars were held at which e-bank representatives presented their credit lines for SME sector.

## Field of the Charter: 9 – Successful E-business models and Top-Class Small Business Support

### Objective:

1. Encourage small enterprises to apply best practice and adopt successful business models that enable them to flourish in the new economy.
2. Develop information and business support systems, networks and services which are easy to access and understand and relevant to the needs of business.

**EPPA Comments:** Within the project *Non-financial Support to SMEs in Serbia* managed by the European Agency for Reconstruction, the study *Potentials for Development and Improving Capacities of SMEs in Serbia for E-business – Preparing the Sector for the Digital Era* was produced, and followed by a conference held on 9<sup>th</sup> March 2004 in Belgrade on this subject, organised in co-operation with the Ministry of Economy.

The main conclusions of the Study and the Conference are the following: improve the telecommunication infrastructure; create a competitive telecommunication market in Serbia; set up an autonomous and independent Republic Agency for Telecommunications; complete the legal environment – enact the Law on E-Signatures, adopt the Law on Intellectual Property; improve access to the Internet; encourage SMEs to participate in e-business; implement the information system of the Republic Government.

An International workshop on Internet and IT development in Serbia was held in Belgrade on 26<sup>th</sup> April 2004, at which current and future trends in use of Internet and information technologies in everyday practice of small and medium-sized enterprises were presented.

## Field of the Charter: 10 – Develop stronger more effective representation of small enterprises' interests at Union and national level

**Objective:** Review how the interests of small businesses are represented at national level, including through the social dialogue

**EPPA Comments:** Under the Labour Law, the Employers Union of Serbia is the social partner and represents interests of employers in the social dialogue which is conducted between employees' representatives – the unions, employers' representatives – the Employers' Union and the Government. SMEs are members of the Employers' Union. The social dialogue that is held within Socio-economic Council at the national level and councils can be formed at local level as well. To date, around 40 local socio-economic councils have been formed at the municipality level.

The *SME Advisory Board* was founded on the initiative of the Government of the Republic of Serbia and with the assistance of EU Project "*Non-financial support to SMEs in Serbia*" managed by European Agency for Reconstruction. The SME Advisory Board was designed as a national forum in which the representatives of public sector and SME sector would sit together and work on solving the issues facing the SME sector. The Minister of Economy and Privatisation appointed the members of the Board. The members of the Board showed a lack of interest in the work of the Board (in 2003, only one session was held) and consequently, an initiative for reviving the Board and the selection of new members has started.

## NOTE

2. European Charter for Small Enterprises - **Report on Small Enterprises in the Republic of Serbia**, according to European Commission Questionnaire for 2004, Ministry of Economy and Privatisation of Republic of Serbia



*Annex V*

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Government and its agencies have a fundamental lead role to play in providing an environment favourable to business operations and conducive to private investment. This is especially true for small business. In order to flourish and grow they need an environment that facilitates and enables business start-up, does not hamper them with excessive and costly regulations and facilitates access to finance and business services.

In 2002 the OECD and the EBRD launched the Enterprise Policy Performance Assessments (EPPAs) in the framework of the Investment Compact for South East Europe (SEE) Programme. The EPPAs consist of a series of reports covering all countries of South East Europe. They assess the quality of government policy for the SME sector and regularly monitor its implementation. The 2004 edition of the EPPAs has been prepared by the OECD and the EBRD in close consultation with the European Commission. Synergies have been created between the EPPA and the European Union Charter for Small Business, covering seven policy dimensions:

- institutional framework;
- regulatory environment;
- tax policy;
- access to finance;
- advisory services;
- business incubators; and,
- entrepreneurship, vocational training and access to technology.

This Enterprise Policy Performance Assessment report is presented as an independent and constructive contribution to the debate on enterprise policy in the Republic of Serbia, bringing forward the views of the small business sector and providing a set of priority actions and policy recommendations to the government and the small business community.