

SMEs and Entrepreneurship Development and Institutional Support in Republic of Srpska (Bosnia and Herzegovina)

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1 Introduction

The economy of Bosnia and Herzegovina and the Republic of Srpska (RS) in the last decade, from 2001 to 2010, according to official statistics, has recorded a significant economic growth. Between 2001 and 2010 GDP in the RS has almost tripled, from 1,478,000 € to 4,250,000 €, respectively (Republic of Srpska Institute of Statistics 2011). This growth is due to the growth of the sector of small and medium-sized enterprises (SMEs) that, in the period between 2006 and 2008, has recorded a growth of SMEs of 8.41 %. The growth has continued in 2009. Out of 14,321 companies, only 55 or 0.38 % were large enterprises. However, in 2010, according to APIF¹ data, 9,472 companies have submitted their required financial reports for the year 2009. Comparing this number with the data from 2009, the question is what happened with other companies? Have they ceased to do business or simply have not fulfilled their legal obligation?

At the beginning of 2009 the first negative effects of the global financial crisis spilled over in the real sector of the RS, which were felt in the decline of the number of companies, job cuts, in the reduction the effective demand, problems of liquidity expressed in low levels of debt collection and the inability to pay short-term obligations, difficulties in accessing external financing sources outside the company, as well as problems with solvency. Economies of developed countries have also felt the negative effects of the recession, but did not give up on further and increased institutional support to SME sector. Small enterprises in the European Union are in fact the true giants of the European economy. Micro enterprises (with fewer than ten employees) are dominant in employment in the countries such as

¹ Intermediary Agency for IT and financial services (abbreviated APIF), <http://www.apif.net/index.php/en>

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Italy (47 %), Poland (41 %), while the share of large enterprises in employment in the Great Britain is only 46 % (Glavanits 2007).

Modern capitalist economies are experiencing a change in the nature of production, organization of work processes and the economic structure (Parker 2001). Traditional, production-oriented industries continue their decline, while service-oriented industry grows and changes (Solymossy 2009). During the economic crisis major companies have released a large number of workers. Mass unemployment and growing poverty have forced governments to revise their interest in big business. Until then, business historians have neglected the SMEs in their research, and very little research in this area has actually been done (Scranton 1984; Benson 1983; Blackford 2003). At the same time, scientific studies have confirmed the importance of SMEs to the economy and this has triggered changes in government policies. According to the highly influential study of David Birch from 1979 as stated by Landström (2005) in his paper, SMEs are largely responsible for creating new jobs, and additional studies have emphasized the high level of innovativeness of SMEs. These figures have shocked many, particularly economists, because it was contradictory to their earlier theories of economies of scale. Further studies have shown that the growth of national income is unambiguously connected with high levels of the foundation of new companies and especially the new so-called start-up companies (Stam et al. 2007; Wong et al. 2005).

While big business was still struggling to survive, and the number of workers was still being reduced, governments wanted and needed to stimulate employment growth. SMEs have been branded as a creator of jobs and the entrepreneur has become a new hero of economic policies. For many this has become the era of entrepreneurship. There is a link between self-employment, entrepreneurship and SMEs, and these are inseparable categories between which there is a strong correlation in the same direction (Goey 2004). *“Small enterprises are the backbone of the Western Balkans economies, according to a report on the implementation of the European Charter in the Western Balkans”* (European Commission Directorate General for Enterprise and Industry 2007, p. 3).

The starting research problem in this chapter can be briefly represented with the question whether the existing institutional support for entrepreneurship development and SME sector in the Republic of Srpska is efficient and enough built? Entrepreneurship is considered to be an important mechanism for economic development through employment, innovation and welfare effects (Schumpeter 1934; Acs and Audretsch 1988; Wennekers and Thurik 1999). The dynamics of entrepreneurship can be vastly different depending on institutional context and level of economic development (Acs et al. 2008).

Analyzing institutional arrangements in the Republic of Srpska, Bosnia and Herzegovina and surrounding countries and European Union, and reviewing the literature of positive European practices, the starting hypothesis of this research can be defined as follows: Improvement of entrepreneurial environment and building of entrepreneurial infrastructure through rounding up the process of building of institutions for financial and non-financial support to SMEs, adopting and implementing policies, programs and strategies, will give an additional contribution

to the establishment of efficient doing business and economic structure of the Republic of Srpska in which SMEs have a dominant role and alongside big giants, will be an engine out of the crisis.

Particular emphasis in this research is placed on the search for answers to following question: which are the key external and internal factors of efficient and effective business of SMEs in the Republic of Srpska? We analyzed the answers of entrepreneurs and managers from 87 SMEs in Banja Luka, administrative centre of Republic of Srpska, in the comprehensive research conducted in late 2009 and early 2010. As a result of the research, we constructed a new *Model of Structural Support to SMEs and Entrepreneurship in the Republic of Srpska*, whose establishment, in the long term, would lead to a systematic and efficient development of entrepreneurship, as well as significant economic growth and employment growth.

2 SMEs Environment in Republic of Srpska

Developed countries are paying more attention to the sector SMEs, through increased investing in entrepreneurial infrastructure and providing a better financial support, which brings as a result well-developed real basis of an economy (Audretsch and Thurik 2001). A special effort in promoting SMEs, which are the main source of economic growth and creation of new jobs, is made by the EU, where 67 % of employed people are in SMEs sector and it accounts for more than 58 % of total turnover (Annual Report on EU Small and Medium sized Enterprises 2010/2011 2012). Development of the competitive position of SMEs in the world primarily depends on their leadership position in the local market. Also, investments in the newest technical and technological achievements are necessary preconditions for development of SMEs as well as their internationalization in order to succeed in the global marketplace. Development of competitiveness arises in the period of a stable industry that encourages the country to find its path in the global market with its perfect product (Porter 1990).

SMEs, as Efendioglu states (2001) constitute the core of the European economy as well as the economy of RS. They are also an integral part of the private sector which contributes significantly to the job creation and plays a key role in enhancing the competitiveness on the target markets, including still underdeveloped markets (Stevenson 2010). Small business in Bosnia and Herzegovina, however, has not been the focus of many scholars; yet, it should be because the environment for small business and entrepreneurship is quite unique there, as Dana (1999, p. 107) quoted. Economy of RS is for many years now in so-called transitional phase of restructuring which is still unfinished. One of the main reasons for this is the lack of promotion of private sector; namely of a slow formation, maintenance, and growth of SMEs. In the period from 2001 to 2010 GDP in the RS almost tripled from 1,478,000 € to 4,250,000 € (Republic of Srpska Institute of Statistics 2011). This growth is in a part due to a growth SMEs sector. However, increase in the

number of new companies which was evident in the period from 2006 to 2008 has been stopped in 2009 as well as the number of companies that are actively operating (Republic Agency for SMEs Development 2010). The number of registered enterprises and the number of companies which are regularly submitting its financial reports to the Agency for IT and financial services (APIF 2012) do not match, indicating a mismatch problem of statistical monitoring of SMEs. It was noted in the Report for 2009 that there were 14,321 in RS, of which only 55 companies or 0.38 % were large companies. However, in the same year according to APIF, only 9,531 companies submitted their financial statements. In 2010 year 9,432 companies submitted financial reports and in 2011 the number was 9,463.

Challenges that the private sector in RS face with are obviously pointing to the fact that it is necessary to take measures to remove barriers to growth and development of the private sector. Therefore, it is necessary to build an adequate supportive business environment and missing entrepreneurship infrastructure for development of SMEs sector. Building of an adequate business environment means building of an environment that will keep existing businesses, and that will be attractive to new domestic and foreign investors. Insufficient usage of attractive locations in the RS that could be activated for the establishment of industrial zones, technology parks, business gardens, business incubators, etc. represent the opportunity costs for RS economy. Here we primarily refer on the non-perspective military facilities, industrial facilities that are not privatized and potential business zones on the future map of network of highways in RS. Supportive business environment implies also completeness of institutional support for entrepreneurial development, financial, consulting, and training as well as the institutions of combined support. Supportive business environment should facilitate the operations of firms, from business registration, obtaining various permits, to the fiscal-stimulating policy, quality system insurance and subsidizing export-oriented enterprises.

Unfortunately, this is not the case in Bosnia and Herzegovina, which has even regressed according to the World Bank's Doing Business Report for 2012. In 2010, Bosnia and Herzegovina was ranked at 116th place of 183 countries in the world in terms of overall ease of doing business, while in 2012 this score was even worse as BH was ranked at 125th place (World Bank 2012). According to the same source (ibid 2012), of the Western Balkan countries, Macedonia is the best ranked country at the 22nd place, Montenegro at the 56th, Slovenia at the 53, Croatia at the 80, Albania at the 82nd and Serbia at the 92nd place. Although the Report of the World Bank (2010, 2011, 2012) cannot be considered completely reliable, however, the data obtained by analyzing the reports of individual countries show that in the Western Balkans, Bosnia and Herzegovina has the most unfavorable environment for starting and running a business and entrepreneurial environment that is rather unsupportive.

Theoretical framework linking the entrepreneurship and economic growth is rooted in the new theories of industrial evolution (Audretsch et al. 2006; Jovanovic 2001; Klepper 1996). "While traditional theories suggest that entrepreneurship will retard economic growth, these new theories suggest exactly the opposite – that entrepreneurship will stimulate and generate growth" (European Commission Enterprise Publications 2003, p. 12).

For the assessment of the position of SMEs in RS, it is necessary to analyze the competition which will be met on the European market. In 2010 in the European Union, of 20,839,226 companies in the private non-financial sector, even 99.8 % of them were small and medium-sized enterprises, of which 92.1 % or 19,198,539 were micro enterprises with up to 10 employees, as it is presented in Table 1.

It can be concluded that insufficient promotion of SMEs sector in the RS, its size and structure, which in the relation to the large companies, do not have an adequate infrastructure and access to various and better sources of funding. "Although the SMEs dominate in the most economies, their smaller size puts them in an unfavorable position compared to larger companies. They have less internal resources and less capacity to compete in the global marketplace" (Stevenson 2010, p. 76). Apart from the internal factors that affect the survival and potential growth of SMEs, there are external factors that affect functioning of this sector as well. In internal factors, among others, we can include entrepreneurial resources, managerial skills, technology, expertise and motivation of the employees. External factors include monitoring of the markets in which enterprise conducts its business, rules and procedures, laws, as well as the regulations that encourage commercial and organizational activities of enterprises (White 2008). In the external factors we can also include monetary and fiscal policy, international economic relations, domestic and global competition, suppliers and the most important factor, customers. More significant progress of SME sector could be expected with planning of big developmental projects in the domestic market, which will be run by local SMEs, relying on their acquired knowledge, experience and skills, all in order to attract domestic and foreign capital, thus creating the basis for export orientation and enhancement of competitiveness.

Further studies have shown that the growth of national income is clearly linked to the high level of new business formation, especially the so-called new start-up companies (Stam et al. 2007; Wong et al. 2005). This unfortunately is not the case in RS, where SMEs are under responsibility of the Department for small and medium-sized enterprises, production and informatics within the Ministry of Industry, Energy and Mining. Other countries of Western Balkans and Central and Eastern Europe, with which we can compare and with which we compete in the regional markets, have ministries that are fully committed to the development of entrepreneurship and SMEs. The last such ministry is the Ministry of Entrepreneurship and Crafts established in Croatia in December 2011 with the advent of the new left-oriented government.

Enterprises need to think about the possibilities of introducing the concept of marketing as a business orientation, entrepreneurial orientation and introduction of total quality management system. In the long term period, by establishing such business orientation and entrepreneurial culture in certain enterprise, intangible assets should provide multiple returns on investment and acquisition of superior competitive position. Apart from the internal factors and satisfactory level of demand for the products and services as one of the major external factors, it is essential that SMEs operate in a stimulating environment in terms of institutional capacities directed to SMEs and business sector in general. Legislative, executive

Table 1 Number of enterprises, employment and gross value added in EU/27, 2010 (estimates)

Enterprises	Micro	Small	Medium	SMEs	Large	Total
Number	19,198,539	1,378,401	219,252	20,796,192	43,034	20,839,226
%	92.1 %	6.6 %	1.1 %	99.8 %	0.2 %	100 %
Employment	38,905,519	26,605,166	21,950,107	87,460,792	43,257,098	130,717,890
Number	29.8 %	20.4 %	16.8 %	66.9 %	33.1 %	100 %
Gross value added	1,293,391	1,132,202	1,067,387	3,492,979	2,485,457	5,978,436
EUR (millions)	21.6 %	18.9 %	17.9 %	58.4 %	41.6 %	100 %

Source: Annual Report on EU Small and Medium sized Enterprises 2010/2011 2012, p. 9

Table 2 The Institutions of support of development entrepreneurship and SMEs in RS

Institutions of financial support of SMEs	Institutions for non-financial and the combined support of SMEs
“Angels”investors	Relevant ministries and departments on the local level
Venture capital funds	Credit-guarantee fund (guarantee fund of the republic of Srpska, city and municipal guarantee funds)
Microcredit organizations	Formal and informal educational institution
Specialized and commercial banks	Consultants (agencies and individual experts)
Factoring companies	Chamber commerce
Banja Luka stock exchange	Professional associations
European union funds and support programmes (CIP, FP7, JEREMI)	Incubators, clusters, technology parks, industrial zones
	Public funds or state-owned development banks (the Republic of Srpska investment-development bank)
	Leasing companies
	Development agencies on the local and national level (Agency for development of SMEs of RS, City Development Agency Banja Luka, University of Banja Luka Entrepreneurship Centre, Innovation Centre Banja Luka, etc.)
	Republic’s funds (development and employment, rural development, etc.)

Source: Authors

and judicial powers are all responsible for creation, sustainable functioning and legality of the instruments of entrepreneurial infrastructure. All institutions can be categorized into two main categories, namely:

1. Institutions of financial support of entrepreneurship and small and medium sized enterprises, and
2. Institutions of non-financial and combined support of entrepreneurship and small and medium sized enterprises.

Comparative review of financial and non-financial institutions of support of SMEs sector and entrepreneurship in the RS on the entity and local level is given in Table 2.

Based on the analysis of the entrepreneurial infrastructure in the Republic of Srpska, we can conclude that we don’t have ministry dealing exclusively with SMEs and entrepreneurs, angels-investors, venture capital funds, factoring companies and technology parks. There are some other instruments and institutions of an entrepreneurial infrastructure, but these are generally underdeveloped and unevenly distributed throughout the territory of RS. Educational system at all levels is not reformed in accordance with European trends which imply introduction of entrepreneurship education at all levels of education.

The problems of SMEs in the RS have relatively recently come into the focus of political and economic public. This raising awareness about the role and importance of SMEs has resulted in their better institutional and legal regulating. In this

regard, for the first time, SMEs are regulated by the adoption of the Law on SMEs development support, and other systemic laws². Until then, small and medium enterprises have not been treated individually, or as a subject of special interest of legislators.

3 Definition of SMEs in the Legislation of the Republic of Srpska

Besides ownership and organizational form of the enterprise, very important factor of one enterprise is its size. Economic criteria are exclusively used in order to divide them into small, medium and large because their effectiveness and efficiency and importance in the overall economy are measured by their actual economic effects. The division of the enterprises is important also for macroeconomic policy with the aim of selective policy of business control and favoring certain forms of enterprises. In the case of RS³, SMEs are treated differently as well as in the Federation of BiH. But, at the level of the state we have no mutually neither coherent legal framework for SMEs, nor these regulations are in the line with European law. Moreover, two laws that define SMEs in the Republic of Srpska are based on different criteria, which can be seen in Table 3.

Unfortunately, these legal decisions that define the same subjects, i.e. small and medium enterprises, in different manner in a single legal framework, may cause confusion in the real sector as well as in the academic community. The following Table 4 presents the basic similarities and differences between legislation in the Republic of Srpska, the Federation of BiH and the European Union.

Legislation in the Republic of Srpska and BiH, which defines SMEs, should be harmonized with the European legislation. Comparative analysis of SME sector in the RS has been done by the SMEs Development Agency of RS in 2010 in the form of report for RS Government. The main deficiency of the analysis, what was highlighted in the report, was insufficient institutional framework for statistical monitoring of data on SMEs and non-use of European methodology according to EUROSTAT. Data from multiple sources have been used, mainly provided by the Pension and Insurance Fond of Republic of Srpska (RS Pension Fund), Agency for IT and financial services (APIF) and the Institute of Statistics, which were often at odds with each other.

Official statistics on the situation in the sector of SMEs in 2011 is published in the form of Report of SME Development Agency to the National Assembly of RS, published in 2012. However, in 2011 according to data of Agency for IT and

²These laws are following: Law on Companies, Law on Guarantee Fund, Law on the single register of accounts of companies, Law on Crafts and Entrepreneurial Activities.

³There are two laws that are contradictory because differentiate differently enterprises by their size: Law on SMEs development support and Law on Accounting and Auditing, as can be seen in Table 3.

Table 3 Definition of SMEs in the legislation of the Republic of Srpska

Law on SMEs development support	Law on accounting and auditing
<p>Article 2</p> <p>SMEs are subject which:</p> <ul style="list-style-type: none"> - employ annually on average up to 249 employees - are independent in business; - make annual total sales revenue up to 50.000.000,00 BAM^a, or have a sum of balance of assets up to 43.000.000,00 BAM. <p>Independency in business according to this Law means that other individuals or legal entities which do not fulfill criteria of the paragraph 1 of this Article, individually or collectively, are not owners of the capital and do not participate in decision-making with more than 25 % in SMEs .</p> <p>Independency in business exists even if there is more than 25 % share in decision-making in the cases:</p> <ul style="list-style-type: none"> - if share in ownership or right of decisions in SMEs has investment found or public sector, under condition that its share in capital or right of decisions, individually or collectively, do not exceed 50 %; - if distribution of shares in capital in SMEs can not be determined, so that, based on statement of an enterprise it can be concluded that other individual or legal entities which do not fulfill criteria of paragraph 2 of this Article, individually or collectively, are not owners of more than 25 %; <p>Article 3</p> <p>Differentiating by their size, there are small and medium enterprises.</p> <p>Small enterprise are legal entities which:</p> <ol style="list-style-type: none"> 1. employ annually on average from 10 to 49 employees 2. make total sales revenue up to 10.000.000,00 BAM, or have sum of balance of assets in the amount up to 10.000.000,00 BAM. <p>Within small enterprises, micro enterprises are differentiated, which employ annually on average less than 10 employees.</p> <p>Medium enterprises are legal entities which:</p> <ol style="list-style-type: none"> 1. employ annually on average from 50 to 249 employees, 2. make total sales revenue up to 50.000.000,00 BAM, or have sum of balance of assets in the amount up to 43.000.000,00 BAM. 	<p>Article 5</p> <ol style="list-style-type: none"> (1) Legal entities are classified according to the average number of employees, total annual revenues and value of asset determined on the date of financial statements in the fiscal year. (2) Based on the criteria in Paragraph 1 of this Article, legal entities are classified as small, medium and large. (3) As small legal entities shall be classified those that meet at least two of the following criteria on the date of the financial statements: <ol style="list-style-type: none"> a) the average number of employees is under 50, b) the average value of assets amounts less than 1,000,000 BAM c) the total annual revenue amounts less than 2,000,000 BAM (4) As medium legal entities shall be classified those that meet at least two of the following criteria on the date of the financial statements: <ol style="list-style-type: none"> a) the average number of employees is from 50 to 250, b) the average value of assets amounts from 1,000,000 BAM to 4,000,000 BAM, and c) the total annual revenue amounts from 2,000,000 BAM to 8,000,000 BAM (5) As large legal entities shall be classified those whose amounts are larger than the largest amounts in at least two of criteria of Paragraph 4 of this Article (6) As medium legal entities are considered also those whose amounts are larger than the largest amounts in one criteria of Paragraph 4 of this Article (7) On the date of financial statements authority of the legal entity independently performs classification in accordance with the above criteria and resulting data is used for the following fiscal year. (8) The newly established legal entities are classified on the basis of the financial statements for the current financial year, in proportion to the number of operating months in business, and resulting data is used for the current and next fiscal year. (9) Average value of operating assets is calculated so the amount of net book value of assets on the beginning of the year and at

(continued)

Table 3 (continued)

Law on SMEs development support	Law on accounting and auditing
	the end of the year is divided by two; average number of employees is calculated so that total number of employees at the end of each month, including those employed outside of RS, is divided with the number of months in the accounting period..
	(10) Notice of classification of the legal entity into category of small, medium or large entities, performed in accordance with the provisions of this Law, shall be submitted by the legal entity to the Agency for IT and financial services (APIF) together with the annual financial statements.
	(11) Notwithstanding the provisions of this Law, banks, micro-credit organizations saving-credit cooperatives, insurance companies, leasing companies, management company of investment funds, management company of mandatory or voluntary pension funds, stock exchanges, broker-dealers and other financial institutions, are considered as large legal entities.

Source: Official Gazette of Republic of Srpska 2009, 2011.

^aBAM is the official currency of Bosnia and Herzegovina <http://www.xe.com/currency/bam-bosnian-convertible-marka>

financial services, 9,432 enterprises submitted its required financial statements for 2010, and in 2012, 9,463 enterprises submitted its required financial statements for 2011. Comparing these numbers with 14,871 enterprises that were registered in 2011, raises a question what happened with about 4,800 companies that have not submitted their financial statements to the Agency for IT and financial services.

It is about 36.36 % decrease in the number of enterprises that exist in the real sector in 2011 compared to the official number of registered companies in 2010 (Table 5).

Data in the table indicate the need for introducing a single business registry in the RS. Namely, the numbers of SMEs in the Republic of Srpska do not match each other, depending on the data source. Data on the economic structure of SMEs show relatively unfavorable structure by activities compared to the structure by activity of SMEs in the European Union. This disadvantage is reflected in participation of the majority of SMEs in three to four economic sectors with a dominant share of retail trade and wholesale trade, repair of motor vehicles and items for personal use, while in the European Union there is a proportional share of small and medium size enterprises in all sectors. The largest number of SMEs in the RS is concentrated in the sector of wholesale and retail trade, repair of motor vehicles and items for personal use (6,018 or 42.18 %), manufacturing (2,898 or 20.31 %), real estate and renting (1,168 or 8.19 %) and in traffic, storage and communications (1,091 or 7.65 %). Large enterprises are most concentrated

Table 4 SME definition in European Union, Republic of Srpska and Federation of Bosnia and Herzegovina

Criteria	European union			Republic of Srpska* (according to the law on SMEs development support)			Federation of Bosnia and Herzegovina		
	Micro	Small	Medium	Micro	Small	Medium	Micro	Small	Medium
Number of employees	<10	<50	<250	<9	<49	<249	<10	<50	<250
Income statement	≤2 mill €	≤10 mill €	≤50 mill €	-	≤5 mill €	≤25 mill €	≤200 000 €	≤2 mill €	≤20 mill €
Balance sheet	≤2 mill €	≤10 mill €	≤43 mill €	-	≤5 mill €	≤21.5 mill €	≤200 000 €	≤2 mill €	≤15 mill €
Independency	More than 25 % of capital or rights can not be controlled by the public institutions			Independency in business according to this Law means that other individuals or legal entities, individually or collectively, are not owners of the capital and do not participate in decision-making with more than 25 % in SMEs					

Source: Official Gazette of Republic of Srpska 2009, 2011

Table 5 Number of SMEs in Republic of Srpska 2007–2011

Year	2007	2008	2009	2010	2011
Number of SMEs (SMEs development agency of RS)	12,391	13,433	14,266	14,482	14,871
Number of active SMEs (APIF)	9,250	9,682	9,531	9,432	9,463

Source: Republic Agency for Small and Medium Enterprises 2012, p. 5

in the sectors of manufacturing and production and supply of electricity, gas and water.

However, in the transitional and developing economies, as is the case with Bosnia and Herzegovina, it is necessary to encourage new entrepreneurial ventures, create new business opportunities, increase productivity and hence competitiveness. It is necessary to create innovation and “induce great players” to invest and thereby increase the future potential of the market, all with the aim of raising the ratings and the potential progress of underdeveloped countries (Sobel et al. 2007). Regardless of whether the economy is developed or less developed country, one thing is certain, that the SME sector is important for the healthy and functioning economy (Ovaska and Sobel 2005). Set high standards that create new business philosophy lead to the conclusion that the transitional countries must be ready to accept new terms and business policies, i.e. to compensate each failed entrance on focused foreign market with strengthening position on the local market.

4 Method, Sample, Instruments and Research Results

Between November 2009 and January 2010, two-stage research was conducted for the purpose of drafting a strategy of small and medium-sized enterprises and entrepreneurship in the city of Banja Luka 2010–2015. The goal of this research was determining influential, stimulating and limiting factors, their direction and intensity on the efficient and effective operations of micro, small and medium-sized enterprises in the City of Banja Luka. City Development Agency with a team of experts in the field of entrepreneurship and small business from the Association of Economists of Republic of Srpska “SWOT” was working on drafting the Strategy for the development of small and medium-sized enterprises and entrepreneurship in the City of Banja Luka, 2010–2015.

The research was conducted using the questionnaire with questions that were designed in a way that they reviewed facts and opinions, and the research had characteristics of both quantitative and qualitative research. The questionnaire consisted of a total of 32 questions, and those were closed questions, questions with several possible answers, questions in the form of answers on the Likert scales, with a descriptive assessment of the attitudes of respondents, and several open questions. The general goal of this research was to enable the authors of the project of drafting the Strategy, whose project team leader was the Sasa Petkovic, one of authors of this paper, on the basis of analyzed influential factors, to define the

strategic goals of strategic determination of the City to build a supportive entrepreneurial environment in the next 5 years, as well as the proposal of specific measures of financial and non-financial support to SMEs in Banja Luka. The research was conducted in two stages.

The first stage was so-called pretesting of the questionnaire stage where, using a method of purposely selected sample of SMEs in the sample of ten companies, we tested the clarity of the questionnaire and the quality of received responses. Of the original 47 questions, after the test stage, the questionnaire was reduced to 32 questions, and in November 2009 the implementation of the research began. The process of data collection was done by a team of the RS Association of Economists "SWOT" solely by electronic means, using their own database of business enterprises in the territory of the City of Banja Luka, using a method of random sample. During the period from 10 November 2009 to 15 January 2010 collection of the questionnaires was conducted directly by sending the questionnaires electronically using a method of random sample, with the degree of response of 24.85 %. The sample included 87 companies from Banja Luka. Questionnaires were sent to about 350 addresses. Interviewers managed to collect 87 questionnaires by double sending questionnaires to the same addresses, with the aim of reminding the respondents. Generally, interest of our businessmen for any type of research is really at a very low level, which certainly makes the job of the academic community more difficult.

In this way, representation of sample is provided, and a sample of 87 SMEs ($N = 87$) compared to the statistical weight is 3.75 % (if we take into account the fact that according to the APIF Report, in 2009, only 2,320 enterprises from Banja Luka submitted their financial statements). In the sample, 32 % of enterprises are "older" than 15 years, 29 % were from 10 to 15 years of age, and only 2 % were established in 2009. From the standpoint of the industry structure, the dominant enterprises in the sample were the ones in the field of retail and wholesale, followed by manufacturing, construction and other industries. Economic structure of the city of Banja Luka, corresponds more to the economic structure of EU average, which is a good indicator of growth and development of the SME sector.

Number of SMEs per 1,000 inhabitants in non-financial business sector of the Republic of Srpska in 2008 amounted to 26.1 SMEs per 1,000 inhabitants⁴, in the region of Banja Luka 30.45 SMEs per 1,000 inhabitants (Analysis of the situation in the field of SMEs for 2008, 2009), and in the City of Banja Luka 47.3 SMEs per 1,000 inhabitants, where the European average of 40 SMEs per 1,000 inhabitants was surpassed. The leading EU countries by number of registered SMEs are Czech Republic (83.4 SMEs per 1,000 inhabitants), followed by Portugal (81.43 SMEs per 1,000 inhabitants), Greece (74.46 SMEs per 1,000 inhabitants), Italy (65.43 SMEs per 1,000 inhabitants) and Spain (60.07 SMEs per 1,000 inhabitants) (Development

⁴The number of enterprises per 1,000 inhabitants was calculated according to the European Commission Recommendation of 6 May 2003 (2003/361/EC)

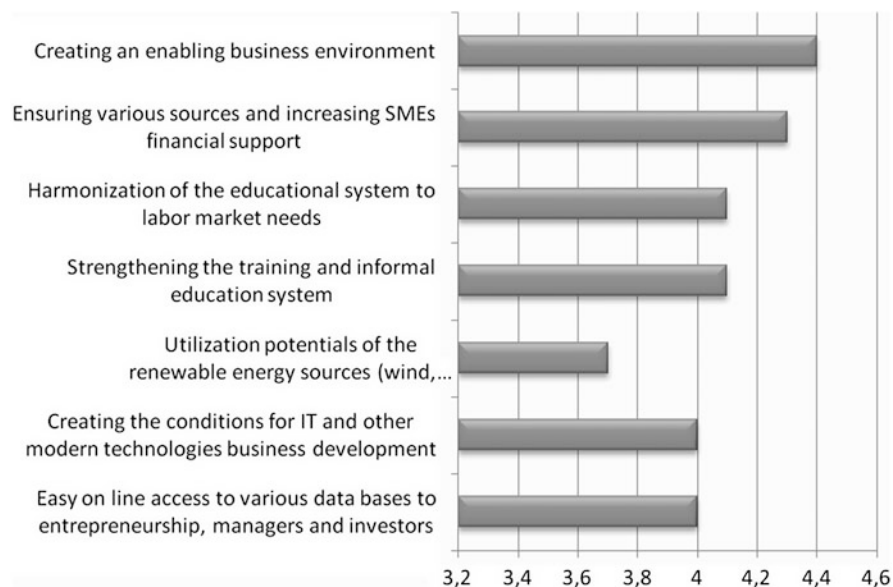


Fig. 1 Attitudes of entrepreneurs from Banja Luka on the priority directions of the development of SMEs in Banja Luka (Source: Authors questionnaire)

Strategy for the SME sector and entrepreneurship in the territory of the City of Banja Luka in the period 2010–2015, 2011).

Given the goal of this research, more attention has been devoted to examining the attitudes of entrepreneurs and managers, rather than on finding cause-effect relationships between the factors of business and total income, and total net profit of the surveyed companies.

Let us return to the goal of this research, which was determining influential, stimulating and limiting factors, their direction and intensity on the efficient and effective operations of micro, small and medium-sized enterprises (SMEs) in the city of Banja Luka. What else have we discovered?

To the question: In your opinion what should be the priority directions in the strategic plan of the development of SMEs in Banja Luka? On the scale from 1 to 5, where 5 marks priority and 1 irrelevant, we got the responses presented in Fig. 1.

Entrepreneurs would primarily like to create a business environment favorable for economic growth and development (weight 4.4), then ensuring and increasing financial support to SMEs (weight 4.3), harmonization of the educational system to labor market needs and strengthening the training and informal education system (both with weights 4.1).

What is significant is the fact that the need for support, both financial and non-financial is evident, and particularly interesting is the interest of entrepreneurs and managers to harmonize the educational system to the needs of enterprises and strengthening the training and informal education system.

Table 6 Limiting factors of SMEs development in Banja Luka

What limits developmental activity in your enterprise? (1 – unimportant, 5 – priority)		
	Responded	Average
The high rate of VAT	67	3.0896
Problems of claims collection	79	4.0759
High rates of taxes and contribution for salaries	74	3.7297
Administrative burdens and complexity of procedures	73	3.6986
The instability and lack of clarity of legislation	70	3.8571
High interest rates of loans	78	4.0513
The costs of energy sources	70	3.5429
Raw materials costs	63	3.2857
Availability of financing sources	70	3.6571
Loss of markets in former Yugoslavia	61	2.6885
Unfair competition	70	3.6857
Foreign competition	63	2.8571
Domestic competition	63	2.8254
Outdated technology	61	2.5246
The quality of products	60	2.9333
Price	63	3.0952
Labor costs	59	3.0000
Outdated products	56	2.9107
Lack of funds for research and development	60	3.2833
Valid N (listwise)	51	

Source: Authors questionnaire

A key part of the research that will partly answer the research problem is related to the research question about obstacles to the development of SMEs. Frequency of the response is summarized in Table 6.

The first problems by priority, with an average score 4.07 and 4.05 were problems of claims collection and high interest rates of loans. These two problems, the problem of claims collection and the problem of reaching the necessary external funds is very important factor that strongly affects the liquidity and solvency of the SMEs in Banja Luka and the Republic of Srpska. Besides the negative effects of the global financial crisis which is evident from the beginning of 2009, inefficient and very expensive judiciary contributed significantly to the first problem. Through the introduction of mediation and the establishment of commercial courts in the Republic of Srpska (the first commercial courts began operating in May 2010) this problem should be less frequent. Further, the instability and lack of clarity of legislation as a very big obstacle for further development of SMEs were assessed with the weight of 3.85. If we compare results across certain studies (Petkovic 2010) and these factors, enterprises do not practice planning (strategic, operational, financial, marketing) in their business operations, so that the uncertainty continues to increase disorientation of the owners and managers of SMEs.

Knowledge to work in conditions of crisis and uncertainty in addition to the natural resourcefulness and intuition must be based on the use of certain forms of

Table 7 Factors of increased competitiveness of SMEs

What needs to be improved in your enterprise in order to be more competitive on the market? (1 – unimportant, 5 – priority)		
	Responded	Average
To improve quality of product/services	70	3.3857
To improve promotion activities	80	3.6250
Get the necessary certificates of the quality	66	2.8788
Professional consultancy assistance in the areas of business and production, e.g. training on specific machine and similar	62	2.6613
Training and education in entrepreneurship	67	3.4925
Training and education in IT	62	3.0484
Training and education in management	69	3.6957
Training and education in project management	64	3.1562
Training and education in finance	65	3.1846
Training and education in sales	70	3.7571
Training and education in marketing	67	3.5970
Training and education in foreign languages	66	3.1970
Associating with companies from my area in order of common market participation	68	3.1912
Assistance from development programmes through grants	78	4.3077
Assistance from development programmes through favorable loans	75	4.3200
Assistance from development programmes through guarantee funds	71	4.2113
Valid N (listwise)	1	

Source: Authors questionnaire

strategic management, which is not applied in our country. High rates of taxes and contributions for salaries (3.72), the administrative burdens and complexity of procedures (3.69) and unfair competition (3.68) are highly ranked barriers to further business development. We would also like to emphasize that the weight of 3.65 evaluated the availability of financing sources as a big problem for SME development in the Republic of Srpska. Finally, with the weight of 3.2 as the limiting factors were assessed the lack of funds for the research and development activities. Thus, the entrepreneurs themselves have noted what they need to improve the competitive position, and which are now the limiting factors in the Republic of Srpska, comparing them with SMEs from the EU. All the factors are external in character. Factors of the external support and internal character, i.e. “inside” the company, according to the respondents, which may affect the further growth and development of SMEs were ranked as follows, as in Table 7.

Entrepreneurs expect assistance from development programs by using favorable loans (4.32), grants (4.30) and guarantee funds (4.21). Thus, there are high expectations in terms of support from government representatives. Few entrepreneurs talked about the need to improve the quality of their products/services (3.38), the need to introduce quality systems (2.87), or the need for professional consultancy assistance (2.66). Therefore, factors of the internal character were rated relatively low. The question for further research is whether the private companies in transition countries should unrealistically expect the full

external help and support from the state for their own development or should they turn to themselves, i.e. to the development of market wanted quality products, innovativity of products or processes, transfer of knowledge, branding, meeting the needs of customers. With respect to the education needs, the greatest need for additional education the entrepreneurs see in the field of sales (3.8), management (3.7) and marketing and promotion activities (3.6).

Absence of statistical significance between the certain variables indirectly confirms the research hypothesis. SMEs do not have an effective system of institutional support to entrepreneurship and SMEs, in the opinion of most respondents:

- Entrepreneurs in Banja Luka do not have available high-quality external resources of financial and non-financial support;
- They are not associated with universities so we cannot talk about the transfer of knowledge and new technologies;
- Most enterprises are not interested in participating in the clusters;
- Entrepreneurs expect assistance from development programs by using favorable loans, grants and guarantee funds.
- Although some entrepreneurs talk about the need to improve the quality of their products/services, the need for the introduction of quality systems and the need for professional consultancy assistance, it is evident the need for education and training in the field of quality and management of SMEs.

Based on analysis of existing legislation, strategies, policies and programs of the support to the development of SMEs and entrepreneurship in the Republic of Srpska, and on an the analysis of the conclusions of the panel discussion on the focus group held in June 2008 and the results of the quantitative research conducted in 2010, we believe that the existing model of institutional support to SMEs in the Republic of Srpska is not adequate, and that the Model of Structural Support to SMEs and Entrepreneurship in the Republic of Srpska, on the example by the cities of the City of Banja Luka, which we suggest can answer to the needs of growth and development of SME sector and changes in qualitative economic structures in Banja Luka and the Republic of Srpska (Fig. 2).

In the proposed *Model of Structural Support to SMEs and Entrepreneurship in the Republic of Srpska*, we propose the reconstruction of ministries in the Government of the Republic of Srpska in accordance with the Constitution of the Republic of Srpska and BiH, taking into account the complexity of the country and political complexity, and territorial compatibility of the Republic of Srpska, geographic area, population, number of regions and relatively simple political arrangement with two levels of government: local and entity. The proposed model of restructuring of ministries was created by the analysis of the model of ministries in Slovenia, Croatia, Serbia and the Czech Republic, where the exceptional institutional attention was given to SMEs. The results are most visible in the Czech Republic, which is the European leader in the number of SMEs per 1,000 inhabitants, a total of 83.4 SMEs per thousand inhabitants (Analysis of the situation in the field of SMEs in the Republic of Srpska 2008, p. 31).

All of the new institutions that should be established are marked in red in the model itself, i.e. they are bold and underlined for easy identification in relation to

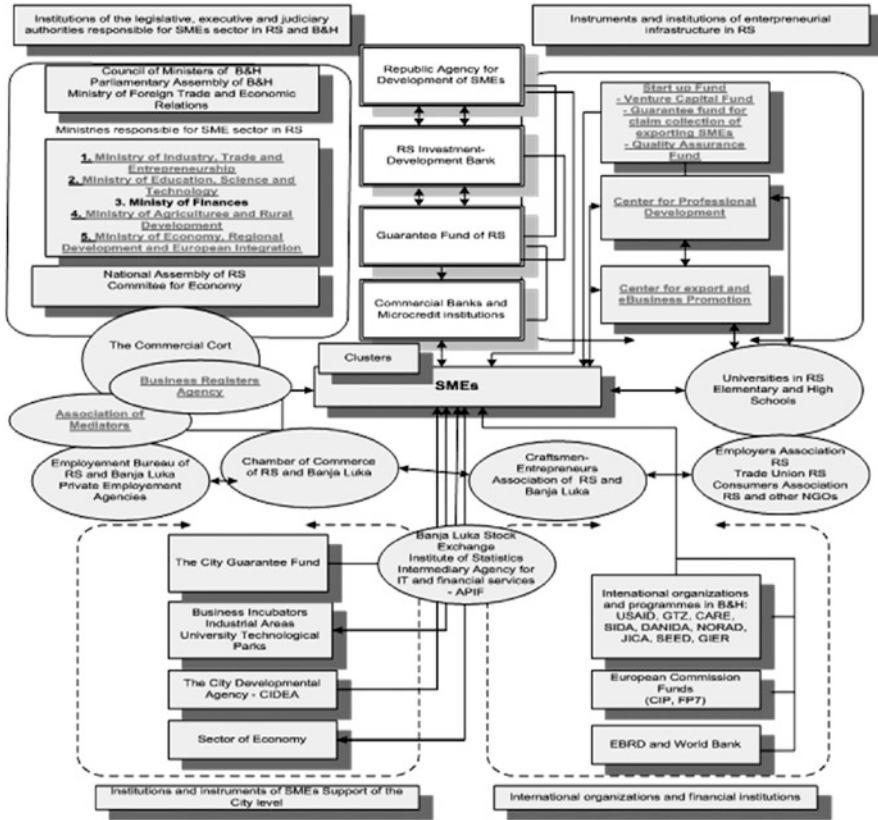


Fig. 2 Model of structural support to SMEs and entrepreneurship in the RS (Source: Authors)

existing institutions. With this regard, in the proposed model, the following ministries would provide direct and indirect support to the development of entrepreneurial environment and SME sectors, namely:

1. Ministry of Industry, Trade and Entrepreneurship.
2. Ministry of Education, Science and Technology.
3. Ministry of Finance.
4. Ministry of Agriculture and Rural Development.
5. Ministry of Economy, Regional Development and European Integration.

Particular emphasis should be placed on strengthening the capacity of the Ministry of Industry, Trade and Entrepreneurship, in case of restructuring the RS Government in the above proposed way. Within the newly established ministry, one part of the ministry that would deal with the entrepreneurship should build its own capacities in a way that in the future it coordinates networking of SME sector and the sector of formal and informal education, local and regional development agencies and entrepreneurs, encourage and assist in the construction of clusters of

SMEs, university and technological parks, business incubators and innovation centers, lobby in the legislature in order to adopt legislation friendly to the development of entrepreneurship and small businesses, involve entrepreneurs in the process of creating new laws and institutional arrangements, help entrepreneurs and clusters in applying for access to European pre-accession funds.

In addition to the RS Guarantee Fund, as the first guarantee pillar of access to loans for newly formed and existing small and medium-sized enterprises, which issued the first guarantees for loans on 08 July 2011, all cities and municipalities need to establish city or municipal guarantee funds, which would constitute the second guarantee pillar for micro and small businesses. Some cities and municipalities already have them, mainly in the northwestern part of the RS, such as Banja Luka, Prijedor, Kozarska Dubica. However, most municipalities have still not established them. The third guarantee pillar should be networks or clusters of small private businesses that would, on the principles of mutual solidarity, guarantee the return of loans from commercial or specialized banks for small and medium-sized enterprises.

The model provides structural support for the establishment of the *Business Registers Agency of the Republic of Srpska* with the aim of quick, cheap and easy business registration. The Agency should provide opening of the web portal for free access to the registry and for online registration of business entities, the electronic cadastre and land registry, documents and forms for public procurement, in the form of “One stop shop”. In accordance with best European practices, business registration process can take up to 7 days, and preferably 48 h. Numerous statistical data on all enterprises would be available at one place, which would be of particular use to the creators of policies, programs and strategies, and scientific workers.

The model proposes the formation of *Start up Fund of the Republic of Srpska* which would consist of the following funds:

- (a) Venture Capital Fund
- (b) Factoring Fund for the purchase of receivables of export enterprises
- (c) Quality Fund

This Fund can be formed within the Investment-Development Bank of the RS, or as an independent legal entity whose founder would be the Republic of Srpska Government.

The purpose of a Venture Capital Fund is to attract “angel” investors and to provide start up capital for promising new companies through the funds of IRB RS. Factoring Fund would participate in co-financing debt collection from the export-oriented enterprises in the Republic of Srpska, which would directly influence the increase in liquidity of SMEs. The objective of the Quality Fund would be to promote the quality culture and assistance in the introduction of various quality systems such as ISO, HACCP, CE mark, etc.

Further encouraging of the establishment of entrepreneurial business incubators, university and technology parks where the future entrepreneurs can get free advice about registration, legal and accounting services and related consulting services, and at relatively low cost start their own business. It is necessary to utilize existing

capacities of the non-privatized industrial enterprises, which do not have the potential for revitalization and ownership transformation and use them to create the above mentioned incubators and parks.

Career Center of the Republic of Srpska would play a role of central training institution for training, additional training and retraining, but also the role of coordinator for the analysis of needs for human resources and labor.

Center for Promotion of Exports and eBusiness would provide support services and subsidies to export-oriented enterprises, and promote the best European practice in eBusiness.

All proposed new institutions for the support to the development of this new structural model should contribute to increasing efficiency and effectiveness of the existing SMEs, accelerate and simplify the creation of new enterprises, enable easy access to information on SMEs and in respect of SMEs to the newly established ministries and institutions, with the aim of systematic surveillance (monitoring) and evaluation of programs, policies and support measures for SMEs.

5 Conclusion

Developed countries, in addition to facing with the global financial crisis, do not give up a systematic search for solutions out of the crisis. In this struggle out of recession, a significant role is played by self-employment and micro, small and medium-sized enterprises. With regard to their basic characteristics, SMEs as flexible, adaptable, relatively inexpensive to establish and close, adjustable to specific market demands, and particularly suited to capture a market niche, with major giants as pillars of the economy should be the generators of economic development. Left on its own without special attention of the state and its institutions, no systematic financial and non-financial support from all sectors, SMEs do not have great chances in the local markets, and especially not in the global market. It is particularly important in transition countries, such as BiH, to continue the positive trend in building institutions that are supporting entrepreneurship and the SME sector. As this research has shown, despite all the positive trends of building entrepreneurial infrastructure in the Republic of Srpska, in the opinion of entrepreneurs and academic community, entrepreneurial infrastructure is still not enough built.

The institutions supporting entrepreneurship and development of the SME sector in the Republic of Srpska do not meet the requirements of entrepreneurs and managers in SMEs. Legislation does not follow the needs of small and in the case of the Republic of Srpska, laws dealing with micro, small and medium-sized enterprises are not harmonized with EU legislation. Larger problem than this discrepancy lies in the internal inconsistency of laws and regulations dealing with SMEs. This is the case with the Law on the Encouragement of the Development of SMEs and the Accounting and Auditing Law, which define SMEs in RS in the diametrically opposite way.

At the RS level, there is no ministry that deals exclusively with entrepreneurs, although in the structure of the RS economy, SMEs dominate with a share of 99.62 % according to data from 2009. Data from the real sector suggest the need for a more serious approach to SMEs. Other ministries in the existing model of the RS Government do not play active role in supporting entrepreneurship. Rather, the SME sector is treated sporadically, and there is a lack of coordinating role of strong ministry that would be solely concerned with SMEs from the real sector.

Given that there is no time to lose, and the negative effects of the global financial crisis are visible, it is necessary in the next 5 years period to get the answers the following questions: How to provide the entrepreneurs in the Republic of Srpska with quality external financial and non-financial support?; how to connect effectively the SME sector with universities so that we can talk about the transfer of knowledge, innovation and new technologies?; how to interest SMEs to join existing or new clusters?; entrepreneurs expect assistance from development programs through favorable loans, grants and guarantee funds. How to continue facilitating access to favorable loans?; although some entrepreneurs talk about the need to improve the quality of their products/services, the need for the introduction of quality systems and the need for professional consultancy assistance in the research, it is evident the need for education and training in the field of quality and management of SMEs. How to build an effective system of formal and informal education of entrepreneurs and managers in SMEs?

Answers to the above questions, arising from the research conducted on a sample of 87 SMEs from Banja Luka, as well as other problems faced by entrepreneurs in the Republic of Srpska due to insufficient development of entrepreneurial infrastructure, in the long-term we can try to solve by implementing the proposed Model of Structural Support to SMEs and Entrepreneurship in the Republic of Srpska. The initial hypothesis of this paper we could check in the future, if the Model is implemented in the Republic of Srpska.

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