

CHAPTER 13. ANALYSIS OF THE LEVEL OF DEVELOPMENT OF PRIVATE SECTOR IN SERBIA DURING THE LAST DECADE¹

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Abstract:

In Serbia, as well as in all the countries in transition, the process of political and economic transition is based on the development of the private sector and entrepreneurship. This also implies creating a favourable business environment for the development of SMEs. The purpose of this chapter is to contribute to our understanding of the private sector and SMEs development in Serbia, as well as to identify their weakness and improvements within the considered period of time. The chapter includes an analysis of various aspects of private sector development as follows: the obstacles to the development, the role of innovation in the private sector growth and the analysis of the role of the private sector in revitalizing Serbia's economy during the last decade. Authors also explain some of the factors which must be taken into account when considering policies for the development of the private sector in Serbia and possible routes forward.

Key words: *SMEs, development, private sector, innovation, business environment Serbia*

INTRODUCTION

In any market economy the SME sector is the primary driver of economic development and employment. Researchers also agree that SMEs are crucial contributors to job creation and economic growth in both high and low-income countries. Consequently, this statement can apply to Serbia where the appearance of the SME sector has been largely linked to privatization and the break-up of large

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State-owned enterprises. Namely, during the last decade Serbia has recognised that the SME sector is of key importance for economic development. In line with this, Serbia has followed the EU trend in developing this sector.

Since 2001, the transition period in Serbia has been accompanied by a number of policy adjustments and an increased urgency to re-align its economic policies to adapt to the new economic order. The reforms have been carried out by the government to support their development as well as many other measures in order to improve the business environment in Serbia. Due to the implemented government reform program to support SMEs, a lot of indicators characterizing this sector improved during the period. Despite certain improvements, however, the SME development has not had such a favourable trend nor has it resulted in improving entrepreneurship activities in a desired manner, due to a negative macroeconomic environment in the country and the recession that hit the national economy (beginning with 2008). Namely, the private sector failed to perform its role as regards absorbing the unemployed workforce that was left redundant as a result of privatization of state-owned companies. Furthermore, no satisfactory results have been achieved as regards new employment, nor is there any increased interest among the unemployed in trying their chances in the private sector of industry.

In order that a more complete and detailed assessment of the trends in the development of the private sector in Serbia be made, this work will primarily focus upon the analysis of the macroeconomic environment, the changes in business demography in the period under consideration, the restraints in the SME development and the characteristics of the business environment. To accomplish this we will make use of the results of our own recent research as well as of the research of others that include a large number of data and analyses. An integral and detailed analysis will serve as basis for suggestions as well as for indicating a direction in which the strategy for the improvement of this sector should be developed. As far as methodology is concerned, we will use the basic methodological principles, applicable to the issue we are dealing with. Thus all epistemological levels of the research will be satisfied – objectivity, system and validity of results. Consequently, we expect that this modest study will be of use to further research in this area and trigger new work. Some of prospective new research will be specifically designated here, in accordance with their importance and priority.

LITERATURE OVERVIEW

The academic literature contains a number of approaches to private sector development, each revealing important aspects of it. Namely, the scientific literature has varied in its scope, methods of analysis and interpretation. In line with this, two

basic sources of economic growth through entrepreneurship can be distinguished in literature, e.g. major established firms, and an entrepreneurial process taking place in new and growing enterprises (early-stage entrepreneurship), (Reynolds et al., 2002). Ayyagari et al. (2006) have analysed firm-level survey data for 80 countries to test which elements of the business environment are the most constraining for enterprise growth. They have found that the lack of financing, street crime, and political instability directly affect the growth rate of firms, whereas taxes and regulations have no significant effect. A World Bank study states that 'rather than directly subsidising SMEs and aiming at a large number of small enterprises, policy-makers should focus on creating a business environment that allows easy entry and exit for firms and assures entrepreneurs and financiers that property rights and contracts will be enforced' (Beck and Demirgüç-Kunt, 2004). In addition, The World Bank's Doing Business Report (2005) has made an important contribution to breaking down 'regulatory burdens' into more operational categories. In fact, empirical evidence suggests that a less bureaucratic business environment fosters economic growth (Altenburg and Drachenfels, 2006). At the same time, UNDP affirms the need for 'a genuine commitment to reform the regulatory environment by eliminating artificial and policy induced constraints to strong economic growth' (UNDP, 2004).

According to Cooper (1981), the decision to start an enterprise in the private sector seems to be influenced by three major factors: (a) the entrepreneurs' background, including the different aspects that have an impact on their motivations and perceptions, such as in their knowledge and skills; (b) the nature of the organization they have previously worked in, which influences the location, nature and the paths of new enterprises; and (c) the factors that generate a climate more or less favourable for founding a new enterprise. Radovic-Markovic and Avolio, (2012c) stressed that the entrepreneurs' background includes psychological characteristics (the need for achievement and the conviction that they can control their own destinies), several family aspects (father or some close relative is owner of his/her own enterprise, the type of education received, and professional experience). They have also pointed out in their research that factors that generate a climate more or less favourable for the formation of new enterprises include the availability of risk capital, economic conditions and business environment, another entrepreneur who acts as model or advisor, the availability of personnel and support services and access to customers.

Survival analysis is commonly used in the economics literature to analyse the determinants of firms' failure (Helmers and Rogers, 2008). Audretsch (1991), who analysed firm survival at the industry level, did include a variable on innovation. He found that survival rates could be higher in more innovative industries. Furthermore many researchers have used patents as an indicator of innovation. As such, patents

have been found to be positively correlated with firms' productivity and market value (Bloom and Van Reenen, 2002, Klette and Kortum, 2004). Thus firms with a larger number of patents should be expected to be more innovative and, therefore, to have a competitive advantage (Helmets and Rogers, 2008). The number of authors who analysed firms' survival found them to be in close connection with universities. According to their research, all firms connected with universities have a lower hazard rate than other firms (Helmets and Rogers, 2008). Hence a better relationship between an education institution and an entrepreneurial activity can contribute to fast information exchange, better access to the most recent knowledge and experiences in this domain and save the time and money (Radović -Marković 2010 a). In addition, Radovic-Markovic (2012a) pointed out that the amount of entrepreneurial activity and willingness to take risks are closely related to a host of possibilities for making profit. The greater the risk, the greater the profitability of a venture has to be to justify the investment. Similarly, if risks are minimised, more investments are likely to be made (OECD/DAC, 2004; the World Bank, 2005). Also, new investments play an important role in increasing the innovativeness of companies and their competitiveness. However, it should be noted that market implementation of innovations largely depends on governments, on general development of entrepreneurship as well as on entrepreneurship in an existing business structure – entrepreneurship (Radović-Marković and Samanzadeh 2012e). A large number of countries focus on the importance of innovation from an economic perspective where entrepreneurship is a driving force for a nation's economic prosperity (Williams, 1983). Accordingly, most literature focuses on the role of innovation in two important respects: a) as a way for organizations to survive and to gain a competitive advantage in a given market; b) as one of the most important national and global general economic growth promoting factors (Tvaronavicius ,V.2011). In line with this, the direct impact of the lack of innovation in SMEs is reflected in the overall international competitiveness (Grozdanic et al., 2012).

Some authors and practitioners have generally assumed that entrepreneurship is the same all over the world. Such notion has changed in recent years when studies started to reveal that entrepreneurship practiced in developing countries was rather different from that in developed countries (Cetindamar 2005). Bearing in mind that each country has its own challenges, opportunities and priorities for change, resources available for implementation will vary by country. Hence the results achieved will also be different. Despite differences among countries, the support for accessing start-up finance is of equal importance for each country and "can have a significant impact on the performance of the enterprise "(Marlow and Patton, 2005). The gap between the required and the available financial resources for entrepreneurial business can be considered in all countries (high and low-income

countries) as the best indicator of the success of SME development policy (Radović-Marković, 2012a).

MACROECONOMIC ENVIRONMENT

The macroeconomic environment of Serbia is based on the promotion of private-ownership. The current macroeconomic environment in Serbia may be assessed as rather poor. Namely, Serbia has an inadequate macroeconomic environment, i.e. Serbia is poorly ranked (at 91th position). This statement is supported by indicators of unfavourable economic conditions in Serbia. There are lots of reasons for this, as follows:

- a) *Low living standard* - In 2012, a family with an average income of 330 euros spent about 41% of their income on food. It is, after Macedonia's, the highest rate in Europe ;
- b) *Low value of average income* – It is close to 330 euros in Serbia (2012). According to the EU standards, each resident with an income below 598 euros is considered poor;
- c) *The high unemployment rate in Serbia* - The labour market indicators reveal negative trends in reducing the overall unemployment rate. It amounted to about 25.5% in April 2012 (in the European Union it is 10. 7%), which is 3.3 percentage points higher than the same month last year and the highest since 1998. Since the outbreak of the crisis in 2008 until now, unemployment has risen by more than 11 percentage points and almost 600,000 people have lost their jobs. This has been the highest unemployment rate in the last 14 years (EurActiv, 2012).
- d) *Account deficit* – It is very high and with a tendency to increase from year to year, which has numerous negative consequences and is not considered to be a sustainable long term condition. According to the data obtained from the Statistical Office of Serbia, the deficit of 5, 228.6 million euros in 2010 increased to 6, 010.3 million euros in 2011. Exports increased from 7, 393.4 million to 8, 439.4 million, however, imports also increased from 12, 622 million euros to 14, 449.7 million (Radović-Marković and Char, 2010).
- e) *Inefficient public administration*- which is usually considered to be a problem for doing business, and which is often linked to corruption.
- f) *Fall in global competitiveness* – this assumption can be explained by a relatively low positioning of the Republic of Serbia. Namely, Serbia is positioned at a relatively low, 95th place on a list of 142 countries, with the Global competitiveness index value of 3.88. This is a fall in comparison with the year 2007, when Serbia was positioned as 91th country (World Economic Forum 2007 and 2011a).

- g) *A low level of Serbian Gross Domestic product per capita in Serbia in relation to EU countries*-Serbian Gross Domestic product per capita, measured according to the purchasing power standards equalled to 35% of the European Union average. According to the preliminary projections of the Ministry of Finance, the rise of the GDP per capita is expected, from 4,518.3 euros in 2011 to 4,799.1 euros in 2012.
- h) *A low level of activity related to innovation* - Serbian innovative activities in comparison to other countries, according to the World Economic Forum's Global Competitiveness Index Rank of 2010 to 2011 (out of 139) are as follows: capacity for innovation ranked 82, quality of scientific research institutions ranked 56, company spending on R and D ranked 108, university industry collaboration in R and D ranked 71, availability of scientists and engineers ranked 92, utility patents per million population ranked 78, availability of the latest technologies ranked 117 and firm-level technology absorption ranked 134. In this context, innovation seems to be a development problem in Serbia (Grozđanić, et.al.2012).
- i) *A high foreign trade deficit* – According to the Statistical Office of the Republic of Serbia, the deficit in foreign trade in the first five months of 2012 amounted to € 2.7 billion, which is a rise by 11.1 percent in comparison to the same period last year.
- j) *An increase in public debt*-At the beginning of the first quarter of 2012, the public debt of Serbia amounted to € 14.6 billion, which is an increase by € 151 million in comparison with the end of 2011, the National Bank of Serbia disclosed. The share of the public debt in the GDP has increased by 3.4 percentage points during the first quarter and now amounts to 51.1 percent, the analysis of the Serbian debt says (Economy.rs, June 13, 2012).

In the 2001-2008 period the Serbian economy realized a rather high rate of economic growth, between 5% and 6% per annum. The growth in economic activities in this period was achieved primarily through the growth in the non-exchangeable goods and services provision sector (trade, banking and financial services, etc.) meant for the home market. Such a model of growth was possible due to a considerable inflow of funds acquired by privatization, from direct investments and foreign loans. Given the economic crisis the first strike of which Serbia suffered in 2008, the capital inflow from loans and foreign investments was reduced. This hindered the economic activity in the country to a significant degree. The drop of the industry sector, trade and construction, led to a fall of 4% of GDP in 2009. This downturn was accelerated by a slow-down in household demand and a high fiscal deficit (Radović-Marković and Char 2010).

PRIVATE SECTOR DEVELOPMENT

Privatisation and SMEs development, decreasing high rate of unemployment and attracting FDI have been within the last decade at the forefront of the Serbian government agenda for economic development. Moreover, Serbia has recognised that the SME sector has been largely linked to privatization and the break-up of large state-owned enterprises. It is also of key importance for market liberalization (UNECE, 2008). A set of privatisation laws enacted in 2001 was meant to ensure the completion of the privatisation of all companies in social ownership by 2010. However, due to the impact of various factors, the privatisation of the remaining public companies and the public sector is constantly delayed. Despite certain delays, however, the privatization process in Serbia planned to be completed by 2012 has already been so. In the privatization of companies Serbia implemented the so-called joint venture model, the so called "flexible model". This model promotes privatisation through strategic partnership and aims to provide new investments, modernization, employment growth, and exports. In that context, the completion of the privatisation of large systems in each of the economic spheres and a more intensive inclusion of SMEs are expected to contribute to the advances in the private sector with all the positive effects in the improvement of competitiveness, innovation and export performance of the Serbian economy (Radović-Marković and Char, 2010).

The privatization process was accompanied by numerous reforms conducted by the state. Namely, since 2001, the transition period in Serbia has been accompanied by a number of policy adjustments and an increased urgency to re-align their economic policies to adapt to the new economic order. The Serbian reform program referred to, among others, reviving economic growth through re-orientation of the country from a public sector-led economy towards increased private sector participation. In line with this, Serbia has followed the EU trend by developing the SME sector in order to reduce the lag in the development of the private sector in comparison to the EU member states.

The intensification of the public companies privatisation process has had a paramount impact upon the dynamics of entrepreneurship activities in Serbia. The tendency of increasing the number of newly established SMEs resulted in the improvement of the business environment, above all creating a macroeconomic stability, the liberalization of foreign trade, the taxation system reform, as well as structural reforms in the field of privatisation.

Table 1: The Privatization Process Results in Serbia in 2002-2009

	2002	2003	2004	2005	2006	2007	2008	2009	Total
Number of sold companies	212	637	236	305	269	309	268	97	2 333
Number of employees in sold companies, in thousands	37.5	76.8	39.3	58.7	45.3	45.9	23.2	8.7	335.5
Sales price (in € mil)	319.3	839.8	154.7	375.4	266.8	403.8	264.8	80.9	2 705.5
Total investments (in € mil)	320.2	319.8	100.0	101.1	294.1	124.9	65.7	43.0	1 368.8
Social programme (in € mil)	145.8	128.3	2.6	0.1	0.0	0.0	0.0	0.0	276.7

Source: Public Finance Bulletin of the Republic of Serbia, January - December 2009

In the space of time from 2002 till 2009, 2333 companies were sold (Table 1). In 2010, only 32 companies were sold, whereas in 2009 three times as many companies were sold (97). The privatized companies increased their incomes by 69% in the period under consideration, whereas the income of unprivatized companies remained on the same level (figure 1). Characteristic of the observed period was a gradual decrease in the number of cancelled privatizations. Also, the income per capita increased 4.3 times in privatized companies.

Failed sales and lack of interest of prospective buyers marked the 2010 and 2011 privatizations in Serbia. According to the data obtained from the Autonomous Trade union of Subotica, the sales in 2010 brought 17.4 million euros and 714 million dinars. The income earned from the sales of the Equity fund shares in 58 companies amounted to € 5.6 million. In 2010, the entire property of 32 companies in bankruptcy was sold, as well as sections of 77 companies. It was in this way that the sum of 1.76 billion dinars was collected (Autonomous Trade union of Subotica, 2010).

Many claim that it is only in privatized firms that the number of employees has fallen in the last decade or so, however, the data disclosed by the Privatization Agency show the opposite. Namely, the number of employees has fallen simultaneously in both privatized and not privatized firms in the period under consideration. In 2002, privatized firms employed 28% of the entire employed population; this percentage was considerably lower in 2010, and amounted to merely 11%. Towards the end of 2011 there were 537 privatized firms in Serbia (Privatization Agency, 2011). The privatization of national economy has not resulted in significant changes in its

structure, primarily due to negative effects of the global crisis that largely devaluated the effects of ownership transformation. The analysis of the privatization in Serbia leads to a conclusion that it has not resulted into the expected economic growth on the basis of business efficiency improvement, but rather in a specific redistribution of income and economic power (AKTER, 2011).

CHANGES IN SME DEMOGRAPHY

The last decade has seen a significant growth of the SME sector in Serbia. According to the data presented by the National Agency for Small and Medium Enterprises, there were 345,000 small (up to 50 employees and up to € 1.65 million of profits) and medium enterprises (up to 250 employees and up to € 8.25 million of profits) and entrepreneurs in Serbia in 2010, which is 12% more in comparison with 2009. SMEs also made up around 92% of all the firms in 2010, employing around 55% of the total number of employed persons and creating around 43% of value added. Thus 9,816 economic entities (companies) were set up in 2010, slightly fewer than a year before when 9,869 companies were established in Serbia. Simultaneously, 10 percent fewer entrepreneurship firms were established in comparison with the year 2009.

In Serbia, the Private Sector is comprised of micro, small, medium, and large enterprises. Small and Medium Enterprises (SMEs) constitute around 99% of all enterprises.

According to the survey of the National Regional Development Agency, conducted by the Republic Statistical Office the majority of firms in Serbia belong to the service sector; a de-industrialization process has been constantly going on since the 1990s. Besides, the analyses of the SME development reveal a tendency of the companies to be generally organized in the form of a limited liability company as this is the most appropriate form of organization for the purpose of conducting entrepreneurship activities in Serbia. The data also depict a rather unfavourable structure of activities, namely, the prevalence of tertiary activities, whereas manufacturing industries are by far less present. The dominant activities are trade, manufacturing industry, real estate and leasing business as well as construction business. Similarly, the regional distribution of the SME sector is uneven. Namely, the regional analysis of the SME development level highlights its concentration and efficient business doing in more developed regions and in big cities.

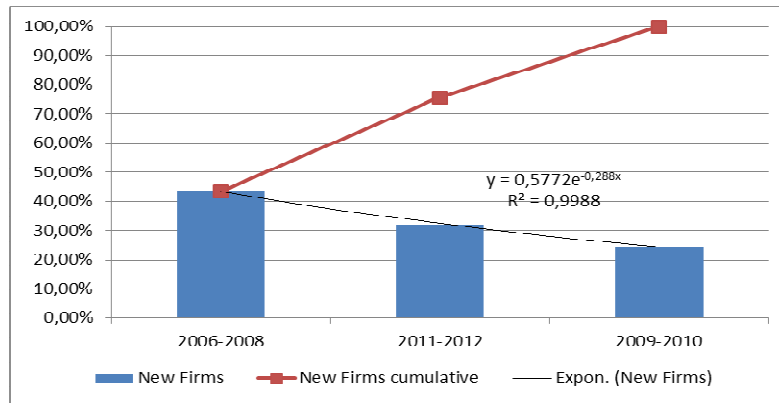
Women entrepreneurs in Serbia are mostly owners of micro enterprises, primarily in the service sector and on local markets. Namely, in as many as 99% cases women entrepreneurs manage the firms that employ fewer than 10 persons, mostly women

(73.4%). According to the latest research conducted by SeCons (2012), these firms are most often (85% cases) registered in a legal form of entity, and in 94% cases the respondents are the sole owners of the firm.

The deterioration in the position of small and medium enterprises can be concluded from a large number of indicators, such as:

- **A larger number of insolvent firms** - In 2008, 30 411 small and medium enterprises were insolvent while in 2011 the number increased to 38 088. In case of entrepreneurs, the total number of insolvent firms rose from 51,799 in 2008 to 91,821 in 2011. (Union of Employers of Serbia, 2012).
- **The low SMEs contribution in employment rate** – Out of a total number of active enterprises in Serbia, almost 99% are SMEs, but their contribution to the employment rate and economical results is considerably smaller compared to developed countries and the European Union. In the analysis of the semi-annual report of the European Commission in 2011, it is highlighted that SMEs development in recent years (with 7 percent participation in employment) does not meet the criteria of the EU, where the participation in employment is 25 percent (Gračanac, A. 2012). The number of employed in 2011 in small and medium enterprises is lower by 61,538 in comparison with 2008.
- **The low technological and innovative level** - Serbian SMEs are aware that they are at low technological and innovative levels, and are faced with the fact that their further development cannot be based on violation of intellectual property rights, but on accelerated path towards the development of entrepreneurial economy based on knowledge.
- **Delays in recovery of outstanding debts** – The average period for the recovery of outstanding debts is becoming longer. In August 2011, it amounted to 132 days. For the sake of comparison, according to the 2010 Eurostat report, the average term of payment in Serbia was 128 days, while in Germany, for example, it was 18 days, in France it was 24 days, while in Croatia it was 34 days (the Chamber of Commerce of the Republic of Serbia, 2011).
- **Lower company survival rate** – Despite the fact that the number of newly set-up small and medium enterprises kept growing, there is an increasing number of those that have gone out of business in recent years. Thus 11,536 firms were established in 2006, while in the first five months of 2012 the number was 12,093. However, while 1,528 firms went out of business in 2006, in 2012 (January to May) the number rose to 14,260 closed small and medium enterprises (Economic Subjects in the Republic of Serbia, 2011). The National Development Strategy assumes that 10,000 more small and medium enterprises should be opened in this country annually than are closed so that Serbia should have 150,000 active small and medium enterprises employing approximately 2 million people by 2016 (Union of Employers of Serbia, 2012). The setting up and closing of small and medium enterprises is shown below (Figure 2 and Figure 3).

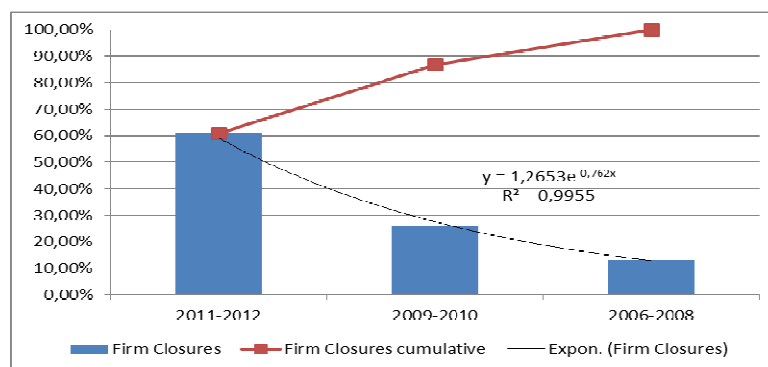
Figure 2: Setting up SMEs in Serbia, 2006-2012.



Source: Data obtained from APR-a, 2006,2007,2008,2009,2010,2011,2012 (I-V)

Despite the big impact the SMEs make in the EU, the growing trends in the last decade have not been recognized in Serbia. Unfavourable economic trends in Serbia that spread to the beginning of 2012 too, resulted into the deterioration of the SMEs position and of the development of entrepreneurship. It is small and medium enterprises and entrepreneurs that pay and will continue to pay the debt incurred by the model through which the state borrowed 7.1 billion euros only in the 2008-March 2012 period and to finance the budget to pay back the debts of the state (Union of Employers of Serbia, 2012). The seriousness of the situation underscores the fact that only 10.45% of small and medium enterprises pay wages on time, and that about 15% have a delay longer than three months. According to the NBS data, 62,234 economic subjects were blocked on 31st September, 2011, the total amount of the blockade being around 182 billion dinars and nearly 94,800 employed (Šoškić, D., 2011).

Figure 3: Closing of SMEs in Serbia, 2006-2012



Source: Data obtained from APR-a, 2006,2007,2008,2009,2010,2011,2012 (I-V)

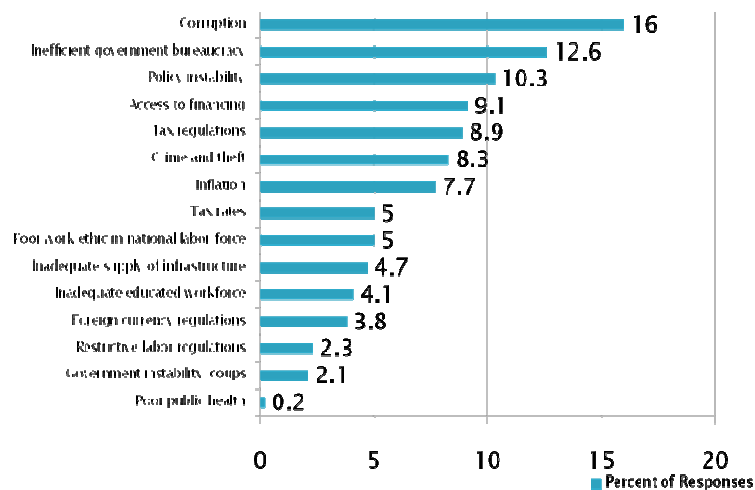
This deterioration in the position affected and will continue to affect the rise in the number of SMEs as well as their survival rate. That was evident in the closing of a large number of SMEs that were unable to cope with the solvency problems, with increased tax burden and other difficulties. Thus, 28,132 small and medium enterprises and entrepreneurs left the VAT system, compared to the number in 2008, which means that their turnover fell below 3 million dinars annually.

Finally, to conclude the above mentioned, we feel certain that the expected results in the domain of the private sector and entrepreneurial activity in Serbia have not been achieved, partly due to following wrong paths in strategies and policy implementation. This resulted into an insufficient growth and prosperity of the SMEs.

MAJOR OBSTACLES TO ENTREPRENEURSHIP DEVELOPMENT IN SERBIA

It is very difficult to carry out entrepreneurial activities in Serbia. The reason lies in the numerous obstacles and limitations, whose effects are extremely discouraging when it comes to meeting these expectations of SMEs. Here we will analyse only a number of obstacles to the development of the private sector and of entrepreneurship, the most important ones in our opinion, regardless of how they are ranked by the World Economic Forum (figure 4).

Figure 4: The most problematic factors for doing business in Serbia



Source: World Economic Forum Global Competitiveness Report 2010-2011

1. Corruption: *The first line of obstacles to doing business refers to corruption (figure 1). Namely, corruption continues to be a worrisome obstacle for private sector development in Serbia. Namely, the citizens of Serbia perceive corruption to be a major problem: the results presented in UNODC report (2011) show that they rank corruption as the most important problem facing their country after unemployment and poverty/low standard of living. According to a research conducted by the USAID in 2011, firms ranked corruption mainly as an issue of personal relationships rather than direct offer of bribe. Almost 90% respondents reported that they had never been in a situation to be set an inappropriate financial requirement by a state servant, whereas 70% reported that they had never given a state servant anything of value, not even a tiny present. More than 50% of respondents, however, claim that they did pull personal connections to accomplish one business or another (USAID, 2011).*

Despite the fact that Serbia introduced important anti-corruption legislation by adopting the Law on Prevention of Conflict of Interests in performing Public Functions (2004), the Law on Corporate Liability for Criminal Acts (2008) and the most recent Law on the Agency for the Fight against Corruption (2010), Serbia's corruption rank continued to rise in 2011 (Table 2).

The fight against corruption remains one of the key challenges in the coming period while the performance of the Serbian Government will be measured against the progress it has made in achieving good governance objectives (Radovic-Markovic and Char 2010).

Table 2: Corruption Perceptions Index (2008- 2011)³

Country	Rank				Score			
	2008	2009	2010	2011	2008	2009	2010	2011
Serbia	85	83	78	86	3.4	3.4	3.5	3.3

Source: Transparency International, Corruption Perceptions Index (issues: 2008, 2009, 2010 and 2011)

The second line refers to a discouraging fiscal and administrative framework for the development of entrepreneurial activities. Although in its Strategy of Development

³ The Corruption Perceptions Index ranks countries/territories based on how corrupt their public sector is perceived to be. A country/territory's score indicates the perceived level of public sector corruption on a scale of 0 - 10, where 0 means that a country is perceived as highly corrupt and 10 means that a country is perceived as very clean (Transparency International)

of Small and Medium Enterprises (SMEs) by 2013 the Serbian government predicted a reduction in administrative costs by at least 25 percent by 2011, just the opposite happened. Thus Serbian entrepreneurs pay three times more taxes than most European countries and those in the region.

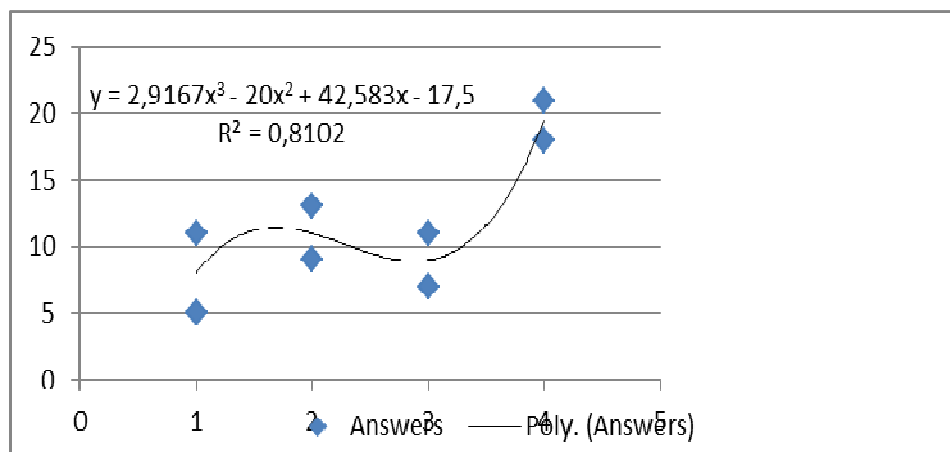
2. Inadequately educated workforce- Any country pretending to have a dynamic economy has to permanently work on improving the competences of its workforce. The Serbian work force is slow to adjust to the changing economic situation. As a result, the demand for skilled employees is increasing faster than the supply (Radović Marković, 2010a). The skill gap can easily explain this statement due to inflexible labour market and missing programmes for specific knowledge and skills. To solve this problem, career counselling and identification of competences and qualifications for an active employment policy should be targeted (Radović Marković, 2010b). Besides, there is no synergy between scientific and educational institutions and the environment. Therefore, the modern business environment should be accompanied by a change in educational environment. Consequently, it is necessary that permanent adjustments between these two environments should be made that will be beneficial for both individuals and the society (Radović Marković, 2012b). This is corroborated by the experts of the Center for Development of Entrepreneurial Society (2010), "weak connection of universities and research and development institutions with the businesses has resulted in insufficient and limited flow of knowledge and know-how, lack of application of scientific and technological research to increase the level of innovation (in the areas of products, production, design, marketing) and modernising technical and technological process of production. It has not been in the function of enhancing the competitiveness of the economy". The recently adopted Strategy of Scientific and Technological Development 2010-2015 aims to encourage cooperation between economy and scientific and research-institutions, i.e. to commercialisation of innovation.

The Europe 2020 Strategy (2010), sets several Initiatives such as "Innovation Union", "New Skills for New Jobs", "Youth on the Move", and "Digital Agenda". In order to efficiently prepare for fast changes in society and work environments, education should provide necessary knowledge and practical skills for students that are trained for management and entrepreneurship.

Recently we have completed a research (Radović-Marković, M. 2012d) which examines two main issues, as follows: (i) How can we encourage the entrepreneurial abilities of students through education? and (ii) In what direction should educational strategies be developed? The research methodology involves carrying out in-depth interviews with respondents from Serbia. The research findings are presented according to the aforementioned research questions. Distribution of the answers is also based on the respondents' gender. After charting the frequency of the answers

in our survey, it was absolutely clear that in all considered countries the entrepreneurial abilities of students can be best fostered in an academic environment by multi-dimensional relationships between course concepts and community-based entrepreneurship experiences. The results also show that there are no significant differences in responses. Namely, most of the respondents (64 out of 95) chose choice 4. Significantly, entrepreneurial abilities of students improvements had a positive effect upon fostering multi-dimensional relationships between course concepts and community-based entrepreneurship experiences, which is showed by regression $y = 2.916x^3 - 20x^2 + 42,8x - 17,5$ (figure 5). The findings on students perceptions regarding the most appropriate direction for the educational strategies to be developed in order to reach the above mentioned goal ,i.e. to encourage the entrepreneurial abilities of students show that most of the respondents (73 out of 95) chose choice 2. According to students' replies, new educational strategies should encourage individuality and freedom of learning, which is showed by regression $y = 2.4167x^3 - 10.5x^2 + 10.083x + 5$ (figure 6).

Figure 5: Distribution of responses for all respondents and considered countries



Source: Radović-Marković, M. (2012d)

Question 1. How can we encourage the entrepreneurial abilities of students through education?

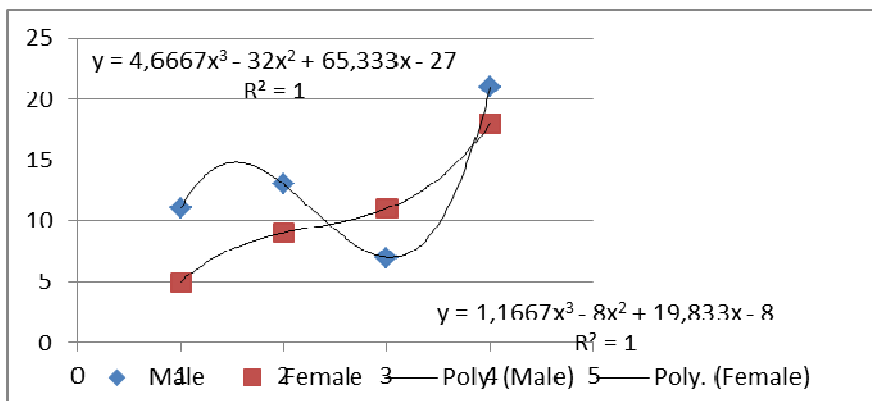
In this question, we were searching for the best choice to encourage the entrepreneurial abilities of students through education. The following choices were provided, according to the qualitative phase:

- 1) Fostering creativity through education
- 2) Offering students the tools to think originally, develop and test their business ideas

- 3) Fostering innovative personality development that creates something unique and turning it into entrepreneurial activity
- 4) Offering multi-dimensional relationships between course concepts and community-based entrepreneurship experiences

Based on the chart it can be seen that there is no differences between the responses by gender (figure 6).

Figure 6: Distribution of responses by gender



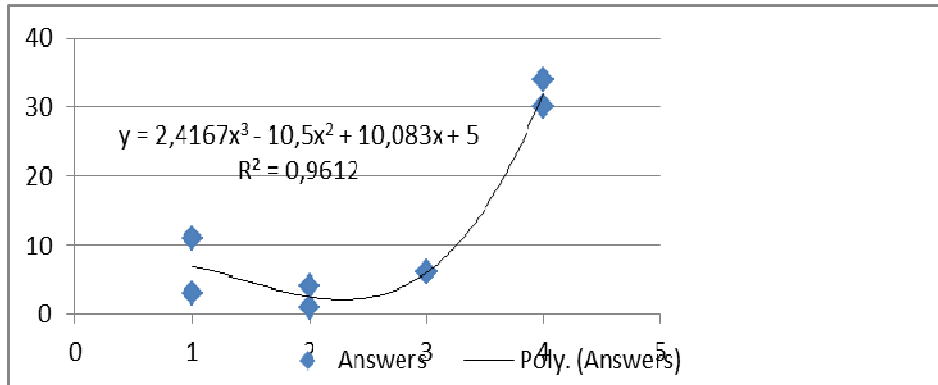
Source: Radović-Marković, M. (2012d)

Question 2: In what direction should educational strategies be developed?

The second question aimed to find the most appropriate direction for educational strategies to be developed in order to reach the mentioned goal to encourage the entrepreneurial abilities of students. Therefore, the following choices were provided based on the in-depth interviews:

- 1) To be more oriented towards the individual needs of students
- 2) To increase an individual's level of independence and freedom
- 3) To increase creative abilities and original thinking
- 4) All of the above

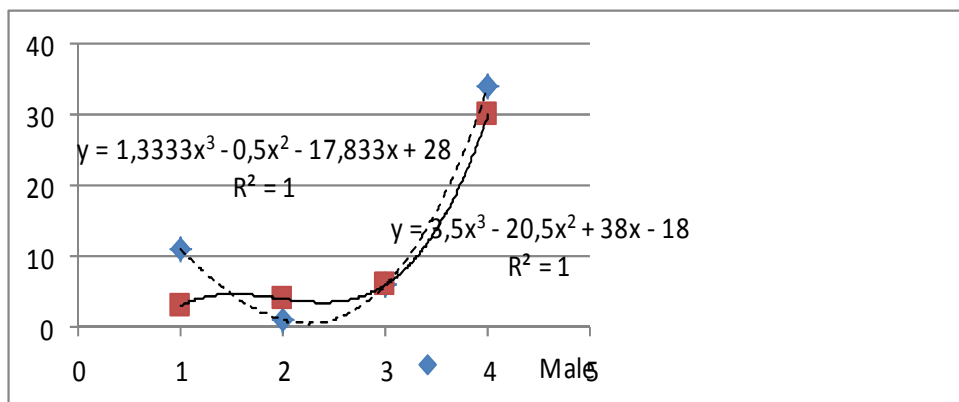
Figure 7: Distribution of responses for all respondents and considered countries



Source: Radović-Marković, M. (2012d)

Chart four shows as well as in chart two, that there are no differences between the responses by gender (figure 8).

Figure 8: Distribution of responses by gender



Source: Radović-Marković, M. (2012d)

Our research shows that the existing education system in Serbia should be redefined and so should educational programs for entrepreneurship. They have to obtain multi-dimensional relationships between course concepts and community based on entrepreneurship experiences. Hence, the creative and interactive education should provide a completely new dimension of gaining knowledge. This active mode of learning allows for the development of innovative personality who creates something unique and turns it into entrepreneurial activity.

3. Access to finance-SME financing has become an important banking market segment in Serbia. Namely, in the times of economic crisis, transition economies are facing numerous challenges in financial markets, thus searching for the most appropriate model for regulating financial sectors. There are only two indicators available to Serbia in this area, neither of which actually measures access to finance and private capital for SMEs. According to the European Commission (2011), it seems that the creditors in Serbia enjoy a higher degree of protection through collateral and bankruptcy laws than in the EU on average, which should generally facilitate lending. At the same time, the indicator measuring the reliability and coverage of public and private credit bureaus which is an important element of a stable financial market is also slightly above the EU average.

According to a large number of experts, the private sector in Serbia and the method of its financing reveal numerous specificities. Primarily, the sources of financing in this sector are limited to a significant degree. Possible financial sources in the Republic of Serbia are loans granted by commercial banks, leasing companies, factoring, microcredit organizations and capital market – corporate bonds, share issuing. The type of financing per life cycle phases is determined by the existing conditions in the region. Consequently, in the conditions of expansion and growth, the investors become interested in investing their money into small and medium-sized enterprises. In the conditions of recession and crisis, however, when aggregate demand declines, small and medium-sized enterprises lose working capital at a fast pace and their solvency is endangered sooner than that of the solvency of large companies. In such circumstances, banks lose their interest in investing into SMEs, unless the state grants some kind of subsidized loans. Hence it is in the conditions of crisis that specific models of financial support to small and medium-sized enterprises emerge, such as “business angels „or “business angels' network“. The notion of business angels is absolutely unknown to as many as 39% of respondents, 24% of them is generally not familiar with it, partly familiar are 20%, whereas only 2% are completely familiar with the notion in Serbia (Eric et al., 2012). It should be particularly stressed here that the today's “business angels „are no philanthropists, they are mainly profit-oriented when investing into SMEs. All the above-mentioned sources of SME financing call for the entrepreneurs to rethink their choices and make their optimum mix. This mix means the combining of own and external financial sources to ensure the achievement of optimum outputs as regards solvency, economy and profitability of firm financing.

Given that SMEs are generally registered in the legal form of private entrepreneur (sole traders) or with unlimited liability or limited liability (more often a case), certain sources from the category of own resources are simply inaccessible to them. According to a recently conducted research on a sample of 600 SMEs in Serbia (Eric et al., 2012), financing on-going activities in Serbia relies on own financial sources. In

case of 35% of the respondents, the ratio between their own (internal) and borrowed (external) sources of finance is 75%: 25%, while 32% of the respondents report this ratio to be 100%: 0%. As few as 17% of the respondents have at their disposal assets from their own sources in amounts equal to the amounts they borrow from external sources, whereas 14% of the respondents state this ratio is 25% : 75%. Credits from the banks are rarely used, since the biggest problems of SMEs in using this type of financing sources are as follows: high interest rates, limited amounts of credits, long and costly procedures of application processing and credit granting, problematic security means. On the basis of this research a conclusion can be drawn that the “adequacy of different sources of financing will depend on the prevailing market conditions, the phase in the SME's life cycle, investment structure, financial standing of the company, the company's goals, money flow stability, management attitude to risk, need for flexibility in managerial decision making, availability of certain sources of financing, type of activity, type and character of the company's business activities.

4. Informal economy -The entrepreneurial sector of the economy of the Republic of Serbia is facing a real problem called Informal economy. Serbia has a large informal sector estimated at 20.6 percent of GDP in 2010, while in the same year its share in the EU is on average 15 percent of GDP (Radović-Marković, M.2010 c). It is fuelled in Serbia by a weak regulatory framework, inappropriate tax and expenditure policies, and weaknesses in law enforcement, including the fight against corruption. It remains an important challenge as it reduces the efficiency of economic policies.

Women are most represented in the structure of informal employment- specifically, those women who have remained outside the process of work. They worked mainly in those industries which are least profitable, or have worked in the informal (residual sector). Often a modest family budget does not afford the ability to start their own business with its own funds or savings, which most women use to start new businesses. Also, there was no help from society-nor are any special purpose loans provided, reflecting the inability of women to reach their undoubtedly entrepreneurial and managerial potential. Therefore, most of them are engaged in marginal jobs in the informal economy or working in some places in the state or socially-owned companies and they aren't in leadership positions (Radovic Markovic, M. 2009c).

5. Inadequate activities of institutions – Institutions in Serbia failed to adequately prepare a favourable environment so that they pass the Act on small business in the future period. According to the research conducted by the members of the Forum of the SMEs of the Chamber of Commerce of Serbia, the attitudes on the conditions for a successful management of small and medium enterprises correlate with the necessity to pass the Act on small business as well as with conceptual and technical

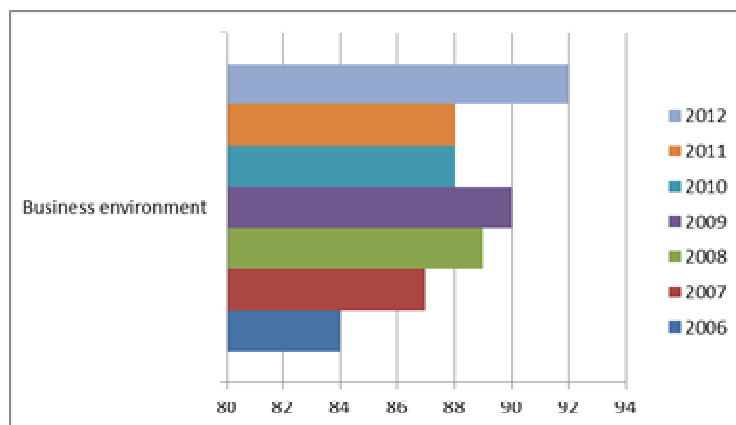
skills of the management. This is of specific importance in today's circumstances when management is faced with a new formula by which the competitive success is based on doing more jobs with less resource. The managers of small and medium enterprises and entrepreneurs will have to go through a period of vigorous activity to preserve their businesses in current conditions and to institutionally and unanimously lobby for the change of legislature.

BUSINESS ENVIRONMENT

Despite the fact that, the National small and medium-size enterprise development strategy for the 2008-2013 period stated that 10,000 more small and medium-size enterprises were planned to be set up than to be closed, this anticipation has already proved to be unrealistic. This is further stressed by the worsened conditions for the development of entrepreneurship in the environment, a consequence of negative economic trends in Serbia. This negative trend was especially determined by the 2008 world economic crisis that affected the economy of this country too.

Surveys of the World Bank have shown a year to year worsening of the business environment of the Serbian economy (from 84 position in 2006 to 92 position in 2012, i.e. change in rank -8 (Figure 9). Compared to the countries of the region, Serbia has a better position than Bosnia and Herzegovina (125). Similarly, according to the data disclosed by the National Agency for Regional Development (2011), Serbia has a lower position than Macedonia (22), Montenegro (56), Romania (72) and Croatia (80).

Figure 9: A cumulative change in Doing Business indicators between DB2006 and DB2012



Source: Data taken from the DB, (2006-2012)

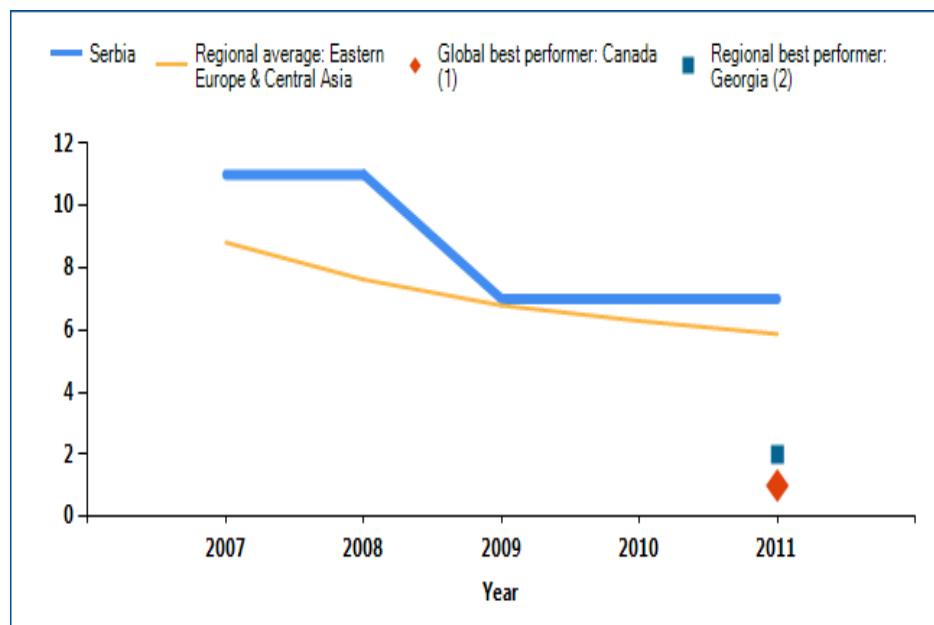
Yearly a cumulative change in Doing Business can provide an indication of changes in a business environment for firms, but does not reflect how the business regulatory environment in an economy has changed over time (Table 3).

Table 3: Ease of Doing Business in Serbia

Ease of Doing Business			
Topic Rankings	DB 2012 Rank	DB 2011 Rank	Change in Rank
Starting a Business	92	81	+11
Dealing with Construction Permits	175	174	+1
Getting Electricity	79	77	+2
Registering Property	39	98	+59
Getting Credit	24	21	+3
Protecting Investors	79	74	+5
Paying Taxes	143	140	+3
Trading Across Borders	79	78	+1
Enforcing Contracts	104	94	+10
Resolving Insolvency	113	91	+22

Source: Doing Business, 2012

Figure 10: Has starting a business become easier over time in Serbia? Procedures (number)



Source: Doing Business database, 2012.

To start a business in Serbia in 2012, 6 different procedures are required, 11 days and 2.8% of gross domestic product per capita is needed. This is an improvement in comparison with 2007, when 11 different procedures were required (figure 2). The greatest improvement in 2012, however, has been made as regards property registering, i.e., Serbia rose from position 98 in 2011 to position 39 in 2012 (table 4). A significant part of the reforms in this area resulted in the reduction of tax on property transfer from 5% to 2.5%.

In order to obtain different types of permits (for construction, power, telephone, inspection or approvals from other agencies, to launch the business, etc., companies are faced with 36 procedures and spend 279 days to complete them (Doing Business, 2012).

As regards the issuance of construction permits, Serbia is at 176th place out of 184 countries, which means among the worst in the world. (Table 5).

Table 4: Dealing with construction permits (easy/difficult Rank), 2012

Easiest RANK	Most difficult RANK
Hong Kong SAR 1	Malawi 174
China 1	Burundi 176
Singapore 2	Serbia 175
Belize 4	Ukraine 179
New Zealand 5	Tanzania 180
Denmark 10	India 177
Georgia 7	Russian Federation 182

Source: Doing Business database, 2012

The situation is similar with taxes payment. Serbia is at 143rd place out of 184 countries. (Table 3).The World Bank study ranked the Serbian business environment as very good for the legal protection of creditors and the amount of data on the loan, as well as for the fact that private credit bureau has data on all adult citizens. However, the World Bank study does not really take into account the sources of credit used.

The execution of the contract has become faster, cheaper and/or less complicated in compared to the situations in 2008 and 2011.As regards enforcing contracts, almost as many as one in three companies that entered the procedure of enforcement of judicial award declare that it took them more than a year to complete the business, whereas one third state that it took them more than three years to do that. Given that court awards are issued slowly, it is necessary that the process of their issuing be made prompter through activating an automatic bankruptcy and in order that the

scope of insolvency should be fully recognized and the blocked capacities be reactivated.

As a result of a regulatory review initiated in 2009, 2,000 laws and regulations were identified as hindering economic activity. This led to the elimination of 192 regulations, while the government approved amendments to laws and regulations in 304 cases. So far, 79 recommendations have been implemented through amendments of 20 regulations and 10 laws. It is estimated that this resulted in annual cost savings to businesses of around EUR 50.8 million (World Bank 2010).

In order to create such a business environment that would be supportive to the development of SME, the Strategy for the Development of Competitive and Innovative Small and Medium-sized Enterprises in the 2008-2013 period was adopted in 2008, with the Operational Plan to implement it, stipulating the basic priorities and the methods for their accomplishment. It means that enabling environment should include functional support mechanism, which in turn involves the activity of the state in defining and implementing the necessary regulations, and support measures to improve the tax system as well as the activities of prominent institutions to support the development of the SME sector. By implementing the Small and Medium-sized Enterprise Development Strategy the state and the local autonomies attempt to improve the institutional and legal business environment and offer the prospective entrepreneurs favourable credit lines for starting up a business, in addition to non-repayable loans. For example, more than 8 thousand firms have been established and 25 thousand jobs have been created since 2007 until the present day using start-up loans granted by the Development Fund (National Agency for Employment, 2012), to give one example. The importance of the state support to the development and stability of this sector is valuable, especially because the entrepreneurship sector was most severely hit by the economic crisis in Serbia, and entrepreneurs' participation in SME is big.

CONCLUSION

We are witnessing great expectations of economic, political and scientific community as regards small and medium enterprises (SMEs) in terms of their impact on the economic development and their capability of generating new jobs, which would significantly reduce the high unemployment rate in Serbia (25.6% in 2012). Also, expectations are expressed in terms of their contribution to innovation, fostering competition, and helping large enterprises increase production efficiency as well as the quality of services in accordance with the requirements of local, national and global market. However, on the other hand, the aforementioned expectations are not adequately monitored and an enabling environment for their

development has not been created. Namely, given that the rating of the business environment for the year 2012 is lower in comparison with the year before, this may have a negative impact upon a further development of the private sector in Serbia. Firstly, as long as this sector is characterised by low competitiveness, an impeded access to finance sources and an undeveloped financial market, a chronic insolvency, an inadequate labour market structure, an uneven regional distribution, an inefficient legislature and a burden of administrative procedures and a high rate of corruption in the administration, it is not realistic to expect that all the potentials of this sector will be well employed in the near future. Serbia's private sector, already heavily taxed and legally restrained, is currently not in a position to absorb newly redundant public-sector workers. It is well obvious now that the state's tendency to cover the budgetary deficit by raising taxes will not result in desired outputs in the economy of Serbia and will restrain the development of the SME sector. Hence it is necessary that a reform of tax system should be conducted, one that would mean the change in the structure of taxation through reducing taxes and dues paid on work but raising the taxes on consumption. Thus the work costs would be reduced and the price competitiveness of all the companies will be improved, whereas the raising of taxes on consumption would additionally burden the imports sector in particular, however the export-oriented manufacture would not be exposed to such additional burden. Also, it should be remembered that the tax system reform would be of great importance for the reduction of the non-formal sector in Serbia.

Although corruption is generally linked with administration, it is increasingly present in the education of Serbia as well. We would like to highlight the issues of inadequate education and corruption that degrades the education system of the country. More than ever before educational institutions become profit-oriented in their struggle to survive, neglecting their basic function – to train quality and adequate personnel, capable of coping with the crisis the modern world is faced with nowadays (Radović-Marković, 2012 d). Hence we witness that educational institutions emerge uncontrollably, offering the same or similar curricula in order to attract as large a number of students as possible, rather than curricula that are geared to the structure and needs of the labour market. Unfortunately, very little research has been carried out to compare the costs of corruption in the education sector. Given that education is the basis of the development of a nation and the survival of the economy, it is necessary that this negative tendency should be curbed as soon as possible (Radović-Marković, 2012 b).

The macroeconomic framework for the 2012-2016 period is focused upon a radical improvement of the business milieu in Serbia that primarily strives to reduce the public expenditure to the level known in the countries on a similar level of development, i.e., with a 35% share in the GDP. Similarly, it is very important to

determine the size of administration and its financing that is acceptable if a desired level of development is to be achieved. A large and too expensive administration hinders many an economy and contributes to its failure, hence this issue must by no means be neglected by our political and economic elites.

Given that the climate for setting up and development of SMEs is not really favourable yet, it is necessary that all the indicators that contribute to this end should be improved (the lowest ranked among which are the issuance of construction permits and enforcement of court orders). Namely, reducing these obstacles is an essential step towards the development of the Private Sector in general, which represents the main objective for all policymakers and practitioners intent on enhancing the business climate in Serbia. This is by no means an easy job, especially not in the conditions of recession that hit Serbia too. Consequently, it is hard to expect that the SME sector will be the driver of economic growth and increase in employment unless the state starts resolving their crucial problems in a more determined manner. The importance of the state support to the development and stability of this sector is valuable, especially because the entrepreneurship sector was most severely hit by the economic crisis in Serbia. The favourable outcomes could be possible to achieve if the activities were jointly conducted by the state and the state institutions on one hand, and the private sector, on the other, all for the purpose of creating new prospects, formulating strategies and opportunities for the development of this sector. The action is needed now and the results can be seen only in the long run.

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