

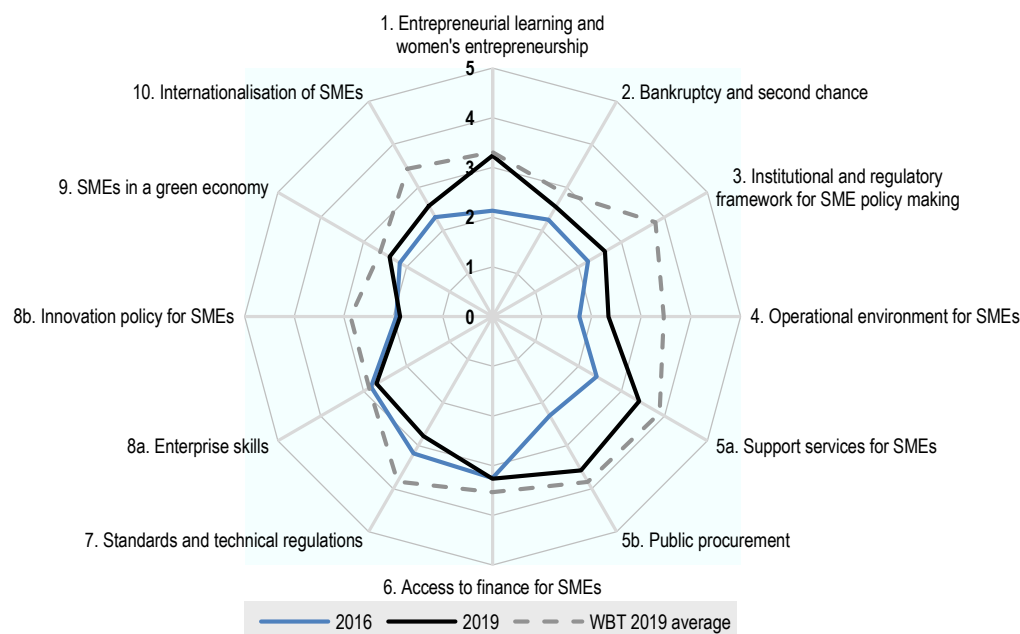
Chapter 14. Bosnia and Herzegovina: Small Business Act profile

This chapter covers in depth the progress made by Bosnia and Herzegovina in implementing the Small Business Act for Europe (SBA) over the period 2016-18. It starts with providing an overview of Bosnia and Herzegovina's economic context, business environment and status of its EU accession process. It then provides some key facts about SMEs in the economy, shedding light on the characteristics of the SME sector. It finally assesses progress made in the 12 thematic policy dimensions relating to the SBA during the reference period, and suggests targeted policy recommendations.

The full version of this chapter is available at <https://doi.org/10.1787/g2g9fa9a-en>.

Key findings

Figure 14.1. Small Business Act scores for Bosnia and Herzegovina (2016 and 2019)



Note: A direct comparison of the scores between the 2016 and 2019 assessments for Dimension 1 (entrepreneurial learning and women's entrepreneurship) and Dimension 8a (enterprise skills) should be treated with caution as the assessment methodology has changed significantly.

Bosnia and Herzegovina has made good progress in implementing the Small Business Act since publication of the *SME Policy Index: Western Balkans and Turkey 2016* (Figure 14.1). Nonetheless, it is still lagging behind its peers in the region. Most of the developments since 2016 relate to the enhancement of the economy's legal and regulatory environment, which has laid the foundations for better SME policy making. The main achievements that have helped Bosnia and Herzegovina improve its performance in this assessment can be summarised as follows:

The introduction of the EU-financed Competitiveness of Enterprises and Small and Medium-Sized Enterprises (COSME) Programme will help to facilitate access to finance and foreign markets for SMEs. The agreement on participation in the COSME Programme entered into force in February 2017. Given BiH's lack of extensive public support mechanisms, the programme could have significant potential to help SMEs access markets in the EU and beyond.

Banking sector regulation and supervision have been strengthened. New banking laws have been passed, aligning the regulations more closely with the Basel framework. These aim to make banks safer and more sound, meaning SMEs in Bosnia and Herzegovina will be less exposed to bank funding constraints in the long term.

Regulatory impact analysis (RIA) procedures have been set up. The obligation to conduct RIAs when adopting laws and by-laws at the state level was introduced in July

2017. Consistent use of RIA could substantially improve evidence-based SME policy making in the economy.

The e-consultation portal has helped to enhance stakeholder engagement. Following the adoption of the Rules for Consultation on Legal Drafting, SMEs are able to provide their input and feedback on legislative proposals through this new website. The number of public institutions using e-consultation increased from 25 in 2016 to 39 in 2018.

The legal framework for insolvency proceedings has been strengthened. The recently prepared bankruptcy laws in the entities include many features that lay the foundation for efficient insolvency procedures. In the Republika Srpska, SMEs in financial difficulty no longer need to file for bankruptcy, and they can initiate debt-restructuring processes. In less than two years, 11 debt settlements were initiated in BiH, saving 600 jobs.

A new Internet portal has centralised all the information for exporters. A new one-stop shop website has been established, providing information on export opportunities, legal regulations and the support measures available to exporting SMEs. Although currently serving only enterprises in the Republika Srpska, this development is an important milestone in supporting enterprises that aim to penetrate foreign markets.

Priority areas

Bosnia and Herzegovina's constitutional arrangements mean that it does not have a unified approach to SME policy planning and implementation, making it challenging to develop coherent policies. Greater co-ordination across all levels of the administration is needed to ensure a whole-of-government approach to SMEs. This report identifies eight priority areas in which Bosnia and Herzegovina should intensify its activities:

- **Take a concerted approach to SME policies.** Due to the constitutional arrangements, there is no overarching framework guiding SME development for the whole economy. The lack of a state-wide SME definition, and the ensuing gap in harmonised data on SMEs and their activities are problematic and obstruct evidence-based policy making. Greater institutional co-ordination of SME policies would enable concerted action and contribute to higher-impact results.
- **Streamline the business registration process.** Each sub-national level of government establishes its own laws and regulations, adding layers of complexity to the business registration process. Entrepreneurs have to register more than once to be allowed to operate throughout the entire territory of Bosnia and Herzegovina. Enhanced co-operation among different levels of government, allowing for the mutual recognition of business registration, would be a good step towards lowering the barriers to entrepreneurship.
- **Continue to embed entrepreneurial learning in school curricula.** As of 2018, only 10% of all primary and secondary schools had embedded entrepreneurship as a key competence in their curricula. All education authorities should cross-reference their curriculum with the European Entrepreneurship Competence Framework and teachers should be trained to meet the revised pedagogic requirements, which will foster a more entrepreneurial culture.
- **Continue digitalising government services for enterprises.** Despite the adoption of new laws, e-signatures have still not been introduced due to the different legal frameworks across the different administrative levels. The number of online services

for enterprises, such as tax payments, needs to be scaled up, and data interoperability ensured.

- **Adopt a whole-of-government approach to establishing quality infrastructure.** The majority of quality infrastructure institutions are understaffed and suffer from limited budgets, hindering the services extended to SMEs. Given these constraints, it is essential to develop a state-wide quality infrastructure system, creating synergies across the administrative levels and avoiding duplication.
- **Foster the uptake of non-bank financing instruments.** Raising awareness of alternatives to bank financing and how they can help SMEs manage their investments and cash flow is important for improving uptake. The reform of the legal framework for leasing along with the new factoring law in the Federation of Bosnia and Herzegovina are expected to contribute to improved uptake. Similarly, a review of the legal framework in Republika Srpska could further boost the take up of alternative sources of financing.
- **Roll out instruments to foster innovation in SMEs.** With the exception of a recently initiated donor programme, there are no public funds available to stimulate SMEs to undertake innovative projects that might be financially risky. A reliable, well-funded financial instrument should be introduced, providing catalytic funding to all BiH SMEs wanting to conduct research and development, develop prototypes and test their ideas.
- **Provide guidance to SMEs in adopting environmentally sound practices.** SMEs need to be nudged to adopt resource efficiency measures. To achieve this, activities are needed to raise SMEs' awareness of how resource efficiency offers high returns for low-cost investments. This would be the first milestone for Bosnia and Herzegovina on its path towards a green economy.

Economic context and role of SMEs

Economic overview

Bosnia and Herzegovina (BiH) is an upper middle-income economy, with a population of 3.5 million and nominal gross domestic product (GDP) per capita of USD 11 714 at current prices in 2017 (World Bank, 2018^[1]). BiH's economy is consumption-driven and one of the most volatile in the Western Balkans and Turkey (WBT) region,¹ with an economic structure that remains highly exposed to external economic fluctuations. The service sector contributes the most value added to the economy, generating 55.8% of GDP in 2017; followed by industry (including construction) at 23.4%; and agriculture, forestry and fishing at 5.8% (World Bank, 2018^[1]). Most of the active labour force was employed in the service (48.7%) and industry (32.2%) sectors, while the agriculture sector accounted for 19.1% of total employment in 2017 (ILO, 2018^[2]).

Public administration² is the third largest economic sector in BiH, constituting over one-fifth of the economy (World Bank, 2018^[3]). The reason for such a high share lies in BiH's particular institutional arrangements which comprise the central government, the governments of the two entities – the Federation of Bosnia and Herzegovina (FBiH) and the Republika Srpska (RS) – the Brčko District, 10 cantonal governments within the FBiH, and local administrations.

The economy has recorded a steady 3% annual growth rate since the last assessment (Table 14.1). This trend continued in 2018 – in the second quarter of which GDP rose by 3.4% year-on-year, up from 2.0% in the first quarter, mainly driven by an increase in private consumption and exports of goods and services (EC, 2018^[4]). In the medium term, growth is expected to pick up even further, provided that structural reforms continue to be implemented by the new government after the state-wide general elections in October 2018 (World Bank, 2018^[3]).

As one of the main drivers of growth, exports rose by 11.9% year-on-year in the second quarter of 2018 (EC, 2018^[4]). This strong performance is largely driven by exports to Germany and Italy, as well as to neighbouring economies – Croatia, Serbia and Slovenia. The European Union (EU) is BiH's main trading partner – contributing 80% of its overall export growth in 2017 (World Bank, 2018^[3]). Mineral products, base metals and machinery are the most important export categories, accounting for more than two-thirds (69%) of export growth in 2018 (World Bank, 2018^[3]). Despite the positive export trend, overall imports have also risen markedly. With no substantial increase in remittances recorded, BiH's current account remains in constant deficit.

Public sector revenues have continued to perform well since the last assessment, with the government registering a surplus of 1.2% of GDP in 2017 (Table 14.1). This was mainly due to improved tax collection and limited spending on public wages. In particular, the February 2018 increase in excise taxes on oil derivatives and the introduction of a road tax and a tax on liquid gas have raised government revenues (World Bank, 2018^[3]). However, this positive fiscal situation seems likely to be short term, given the government's latest announcement of new spending measures. In particular, in 2018 both falling tax revenues and increased spending on wages, social transfers and investment were expected to increase the need for lending, causing a deficit of 0.5% of GDP (World Bank, 2018^[3]). This is why, in July 2018, the International Monetary Fund (IMF) postponed a discussion on the planned disbursement of the Extended Fund Facility Support Programme's next tranche of around EUR 38 million, due to the need to reassess the country's fiscal position (EC, 2018^[4]).

Foreign direct investment (FDI), at around 2% of GDP, is one of the lowest in the WBT region, remaining a weak source of investment in the country. Investors are discouraged by fragmented and poorly functioning product and labour markets, the weak rule of law and a continuing poor business environment (EC, 2018^[5]).

On a positive note, however, the banking sector remains liquid, with the share of non-performing loans steadily falling from 11.1% in 2017 to 9.3% in the second quarter of 2018 (EC, 2018^[4]). Inflation remains low, at 1.2% in 2017 (Table 14.1), but rose to 1.8% in August 2018, driven by higher prices for tobacco, transport, housing and healthcare (EC, 2018^[4]).

Unemployment in Bosnia and Herzegovina continues to be relatively high, the third highest in the WBT region after Kosovo* and the Republic of North Macedonia. However, unemployment fell from 25.4% in 2016 to 20.5% in 2017, supported by a slight increase in employment in the manufacturing, wholesale trade and tourism sectors. Nevertheless, BiH remains the only Western Balkan (WB) economy where employment is yet to recover to the levels seen before the 2008 crisis; the employment rate in 2017 was about 8% lower than in 2008 (World Bank, 2017^[6]). The people most affected by high unemployment are 55-64 year-olds and the more highly educated (OECD, 2018^[7]). In addition, high youth unemployment (of over 60%) and high levels of long-term unemployment (82% of all unemployed people) remain major sources of concern, as noted in the previous assessment (EC, 2018^[4]; World Bank, 2018^[3]). Youth unemployment continues to contribute to an endemic brain drain from the country.

Table 14.1. Bosnia and Herzegovina: Main macroeconomic indicators (2013-18)

Indicator	Unit of measurement	2013	2014	2015	2016	2017	2018
GDP growth ¹	% year-on-year	2.6	0.2	3.8	3.3	3.4	2.7**
Inflation ¹	% average	-0.1	-0.9	-1.0	-1.1	1.2	1.1
Government balance ¹	% of GDP	-2.0	-2.0	0.6	1.2	2.5	..
Current account balance ²	% of GDP	-5.3	-7.4	-5.4	-4.9	-4.8	-6.0*
Exchange rate BAM/EUR ¹	Value	1.96	1.96	1.96	1.96	1.96	1.96***
Exports of goods and services ¹	% of GDP	31.8	32.8	33.6	34.4	39.4	40.2**
Imports of goods and services ¹	% of GDP	51.1	54.6	51.4	50.5	55.5	56.2**
Net FDI ¹	% of GDP	1.2	2.8	1.7	1.6	2.0	2.0**
External debt ²	% of GDP	61.7	61.6	62.3	62.4	61.0	..
Gross international reserves ¹	% of GDP	5.5	5.9	6.3	7.2	7.0	6.5
Unemployment ¹	% of total active population	27.5	27.5	27.7	25.4	20.5	..
National GDP ³	EUR billion	13.70	13.99	14.62	15.29

Note: *: projection; **: average of 1st and 2nd quarter; ***: average of the 1st, 2nd and 3rd quarter.

* This designation is without prejudice to positions on status, and is in line with United Nations Security Council Resolution 1244/99 and the Advisory Opinion of the International Court of Justice on Kosovo's declaration of independence.

Sources: ¹ EC (2018^[4]), “EU candidate countries’ and potential candidates’ economic quarterly (CCEQ): 3rd quarter 2018”, <http://dx.doi.org/10.2765/319761>; ² EBRD (2018^[8]), *Transition Report 2018-2019: Work in Transition*, <https://2018.tr-ebd.com/downloads/>; ³ Eurostat (2018^[9]), *Eurostat (database)*, <https://ec.europa.eu/eurostat/data/database>.

Business environment trends

A regulatory and institutional environment which facilitates doing business is a necessary pre-condition for small and medium-sized enterprises (SMEs) to thrive. Despite a positive economic outlook, the business environment in Bosnia and Herzegovina remains highly burdensome. As outlined in its Economic Reform Programme 2018-2020 (Box 14.1), the major reasons for its poor private sector performance stem from a complex institutional set-up, which has created a large and inefficient public sector that dominates the economy.

The significant obstacles identified in the ERP can be summarised as the continuing lack of a single economic space; weak access to finance; weak rule of law; and the complex, unclear and sometimes contradictory legal and regulatory frameworks (EC, 2018^[5]; BiH, 2018^[10]). In addition to the significant cost of business entry and exit procedures, businesses are subjected to numerous para-fiscal charges. Gaps in contract enforcement and implementation of laws further aggravate the business environment (BiH, 2018^[10]).

According to the OECD *FDI Regulatory Restrictiveness Index* (OECD, 2017^[11]), Bosnia and Herzegovina is one of the most open to FDI of 68 economies assessed, including OECD and some selected non-OECD countries (OECD, 2018^[7]). It maintains only a few restrictions, making its FDI regime less restrictive than that of an average OECD economy or the 22 EU Member States covered by the index.³ However, it still has to establish comprehensive programmes to create better linkages between foreign investors and domestic firms to enhance the impact of FDI (OECD, 2018^[7]).

The widespread informal economy poses another burden on doing business in BiH. This particularly affects SMEs, as the incidence of informality decreases as firms get larger due to the higher costs of regulatory compliance for smaller firms. BiH also performs poorly in terms of corruption levels. With a score of 38 in Transparency International’s 2018 *Corruption Perceptions Index*, the country is ranked 89th out of 180 countries and territories (Transparency International, 2019^[12]).

One of the additional vulnerabilities of the business environment is the preferential status often granted to its state-owned enterprises. In particular, unlike other WBT economies, BiH has numerous statutory corporations which are subject to treatment that may differ from ordinary corporate norms, giving them undue advantages over private enterprises (OECD, 2018^[7]).

Challenges like these were widely expressed in the interviews conducted with SME owners and entrepreneurs in BiH as part of the SBA assessment. The interviewees also emphasised the complexity of procedures related to the business sector and SMEs. They highlighted that setting up a business and obtaining business licences and approvals for construction were particularly burdensome. They did underline one positive achievement in business licensing: a significant number of municipalities in BiH have published written procedures and guidelines for business licensing on their websites, making the procedure clearer and more transparent than in the previous assessment period.

Box 14.1. Economic Reform Programmes

Since 2015, all EU candidate countries and potential candidates are obliged to prepare Economic Reform Programmes (ERPs). ERPs prepare the enlargement countries for their future participation in the EU's economic policy co-ordination procedures. They also play a key role in improving economic policy planning and steering reforms to sustain macroeconomic stability, boost competitiveness and improve conditions for inclusive growth and job creation.

The ERPs contain medium-term macroeconomic projections (including for GDP growth, inflation, trade balance and capital flows), budgetary plans for the next three years and a structural reform agenda. The structural reform agenda includes reforms to boost competitiveness and improve conditions for inclusive growth and job creation in the following areas:

1. public finance management
2. energy and transport markets
3. sectoral development
4. business environment and reduction of the informal economy
5. trade-related reform
6. education and skills
7. employment and labour markets
8. social inclusion, poverty reduction and equal opportunities.

The European Commission and the European Central Bank then assess these seven programmes. This forms the basis for a multilateral economic policy dialogue involving the enlargement countries, EU Member States, the Commission and the European Central Bank. The dialogue culminates in a high-level meeting during which participants adopt joint conclusions that include country-specific policy guidance reflecting the most pressing economic reform needs.

The findings of the Small Business Act assessment for the Western Balkans and Turkey provide the analytical background and guidance to the seven EU candidates and potential candidates in identifying the key obstacles to competitiveness and economic growth, and in developing structural reform measures to overcome them.

Source: EC (2018^[13]), *Economic Reform Programmes: Western Balkans and Turkey*, <https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/20180417-erp-factsheet.pdf>.

All in all, Bosnia and Herzegovina has dropped three places in the World Bank's *Doing Business 2019* report compared to the previous year, and was ranked 89th out of 190 countries – the lowest ranking in the WBT region (World Bank, 2018^[14]). The most pressing issues remain dealing with construction permits, starting a business and paying taxes (World Bank, 2018^[14]). BiH has made paying taxes easier by abolishing the tourist community fee and has also made some progress on making it easier to start a business (World Bank, 2018^[14]). Table 14.2 highlights the most recent business reforms.

Table 14.2. Recent business reforms in Bosnia and Herzegovina

	Reforms making it easier to do business	Reforms making it harder to do business
Doing Business 2017	<p>Made it easier to start a business by reducing the paid-in minimum capital requirement for limited liability companies and increasing the efficiency of the notary system.</p> <p>Facilitated paying taxes by abolishing the tourist community fee.</p>	None

Note: Only reforms which had either a positive or a negative impact on conducting business were considered.
Source: Adapted from the World Bank (World Bank, 2018^[15]) *Business Reforms in Bosnia and Herzegovina*, www.doingbusiness.org/en/reforms/overview/economy/bosnia-and-herzegovina.

EU accession process

During the Thessaloniki European Council Summit in June 2003, Bosnia and Herzegovina was identified as a potential candidate for EU membership. The co-operation between the EU and BiH advanced further following the Stabilisation and Association Agreement (SAA), which entered into force 12 years later in June 2015. The SAA constituted a comprehensive framework for closer political dialogue between the EU and BiH, and for establishing a free trade area.

In February 2016, BiH applied for EU membership, and in September 2016 the European Council invited the European Commission to submit its opinion on the merits of this application (EC, 2018^[16]). The questionnaire covering all EU accession criteria was then handed over to BiH, whose consolidated answers were finalised in February 2018 and sent to the President of the European Commission. In June 2018, BiH received follow-up questions from the Commission; it has yet to submit the additional information requested at the time of writing. The Commission will prepare its opinion based on the answers to the questionnaire, peer reviews and consultations with international organisations and civil society.

Bosnia and Herzegovina has continued to implement the SAA and the meetings of the joint bodies under the agreement have taken place, except for the Stabilisation and Association Parliamentary Committee which has yet to adopt its Rules of Procedures (EC, 2018^[16]). The EU and the BiH authorities meet annually to discuss a wide range of policy issues and agree on follow-up actions. Progress reports assess the readiness of BiH to move closer to the EU. The findings and recommendations published in the *SME Policy Index: Western Balkans and Turkey* provide the monitoring and guidance needed for BiH to prepare and meet the requirements related to their potential candidate status under “enterprise and industrial policy”.

According to the latest progress report, published in April 2018, BiH has made some progress in the business environment area (EC, 2018^[16]). In particular, it has slightly improved its market entry and exit regulation and continued its efforts to facilitate business registration.

EU financial support

The EU is the largest provider of financial assistance to BiH. Between 2007 and 2013, it received a total of EUR 615 million under the first phase of Instrument for Pre-Accession Assistance (IPA) (Delegation of the European Union to Bosnia and Herzegovina, 2018^[17]). The second phase, IPA II, will allocate a total of EUR 2.9 billion for the period

2014-20 (including EUR 542 million in unallocated funds for BiH), whereas EUR 165 million was distributed in the first stage (Delegation of the European Union to Bosnia and Herzegovina, 2018^[17]). IPA support in BiH is conditional upon it adopting key state-wide strategies (i.e. for the whole economy, including all the entities). The sector strategies for the environment, adopted in May 2017, and for rural development, adopted in February 2018, enabled IPA financing in those sectors. In order to fully benefit from IPA II funding for 2018-20, BiH will need to adopt state-wide strategies for public financial management and employment (Delegation of the European Union to Bosnia and Herzegovina, 2018^[17]).

In 2017, BiH joined the EU's COSME financing programme. The following year, the European Investment Fund (EIF) and Procurement Bank established a guarantee agreement to support SMEs in Bosnia and Herzegovina via a guarantee mechanism under the Western Balkans Enterprise Development and Innovation Facility (WB EDIF). The Western Balkans Guarantee Facility agreement has so far provided EUR 22.7 million in SME loans, financing a total of 144 SMEs in BiH (WB EDIF, 2018^[18]).

In addition to the EU assistance funds, BiH has received EUR 2.2 billion in European Investment Bank loans since 1999, and another EUR 122 million in Western Balkans Investment Framework grants since 2009, leveraging investments estimated at EUR 2.8 billion (EC, 2018^[19]).

SMEs in the national economy

In accordance with the division of administrative competencies, the legal definition of SMEs is decided at the entity level in BiH. Each entity has two definitions of SMEs: one in the Law on Accounting and Auditing for accounting purposes, and another in the Law on Fostering Small Business Development in the FBiH (Table 14.3) and Law on SME Development in the RS (Table 14.4) for the purposes of providing financial support to SMEs. In addition, the Brčko District has its own SME definition in the Law on Enterprises (Table 14.5).

The definition for accounting purposes is the same in both entities and distinguishes between small, medium-sized and large companies. The Law on Accounting and Auditing provides clear criteria for micro enterprises in the RS, whereas the FBiH does not define them separately. Since the last assessment, the RS has reduced the turnover and balance sheet thresholds in its second SME definition so as to harmonise them with the first, which has made the two entities' definitions more comparable and coherent according to both laws.

For the purposes of financial reporting, the two entities' accounting and auditing laws use financial thresholds to categorise SMEs that differ from those in the EU definition, although the employment criteria are the same. These definitions are adapted to the specific context of the economy of each entity.

Table 14.3. Definition of micro, small and medium-sized enterprises in the Federation of Bosnia and Herzegovina

	EU definition	Law on Accounting and Auditing	Law on Fostering Small Business Development
Micro	< 10 employees ≤ EUR 2 million turnover or balance sheet	No definition in place	< 10 employees ≤ BAM 400.000 (~EUR 204 000 turnover and/or balance sheet
Small	< 50 employees ≤ EUR 10 million turnover or balance sheet	< 50 employees < BAM 1 million (~EUR 0.51 million) circulating assets < BAM 2 million (~EUR 1.02 million) turnover	< 50 employees ≤ BAM 4 million (~EUR 2.04 million) turnover and/or balance sheet
Medium-sized	< 250 employees ≤ EUR 50 million turnover ≤ EUR 43 million balance sheet	< 250 employees < BAM 4 million (~EUR 2.04 million) circulating assets < BAM 8 million (~EUR 4.08 million) turnover	< 250 employees ≤ BAM 40 million (~EUR 20.41 million) turnover and/or ≤ BAM 30 million (~EUR 15.30 million) balance sheet

Note: BAM: Bosnia and Herzegovina convertible mark; exchange rate as of December 2018.

Sources: FBiH (2009^[20]), *Zakon o računovodstvu i reviziji u Federaciji Bosne i Hercegovine (Law on accounting and auditing)*, https://advokat-prnjavorac.com/zakoni/Zakon_o_racunovodstvu_i_reviziji_FBiH.pdf; FBiH (2006^[21]), *Zakon o poticanju malog gospodarstva (Law on fostering small business development)*, www.fmrpo.gov.ba/dokumenti/zakoni/.

Table 14.4. Definition of micro, small and medium-sized enterprises in the Republika Srpska

	EU definition	Law on Accounting and Auditing	Law on SME Development
Micro	< 10 employees ≤ EUR 2 million turnover or balance sheet	< 5 employees < BAM 250 000 (~EUR 128 000) balance sheet < BAM 500 000 (~EUR 255 000) turnover	< 10 employees
Small	< 50 employees ≤ EUR 10 million turnover or balance sheet	< 50 employees < BAM 1 million (~EUR 0.51million) balance sheet < BAM 2 million (~EUR 1.02 million) turnover	< 50 employees < BAM 1 million (~EUR 0.51 million) balance sheet ≤ BAM 2 million (~EUR 1.02 million) turnover
Medium-sized	< 250 employees ≤ EUR 50 million turnover ≤ EUR 43 million balance sheet	< 250 employees < BAM 4 million (~EUR 2.04 million) balance sheet < BAM 8 million (~EUR 4.08 million) turnover	< 250 employees ≤ BAM 4 million (~ EUR 2.04 million) balance sheet ≤ BAM 8 million (~ EUR 4.08 million) turnover and/or

Note: BAM: Bosnia and Herzegovina convertible mark; exchange rate as of December 2018.

Sources: RS (2013^[22]), *Zakon o razvoju malih i srednjih preduzeća (Law on SME development)*, https://advokat-prnjavorac.com/zakoni/Zakon_o_razvoju_malih_i_srednjih_preduzeca_RS.pdf; RS (2015^[23]), *Zakon o računovodstvu i reviziji Republike Srpske (Law on accounting and auditing)*, <https://advokat-prnjavorac.com/zakoni/Zakon-o-racunovodstvu-i-reviziji-Republike-Srpske.pdf>.

Table 14.5. Definition of micro, small and medium-sized enterprises in the Brčko District

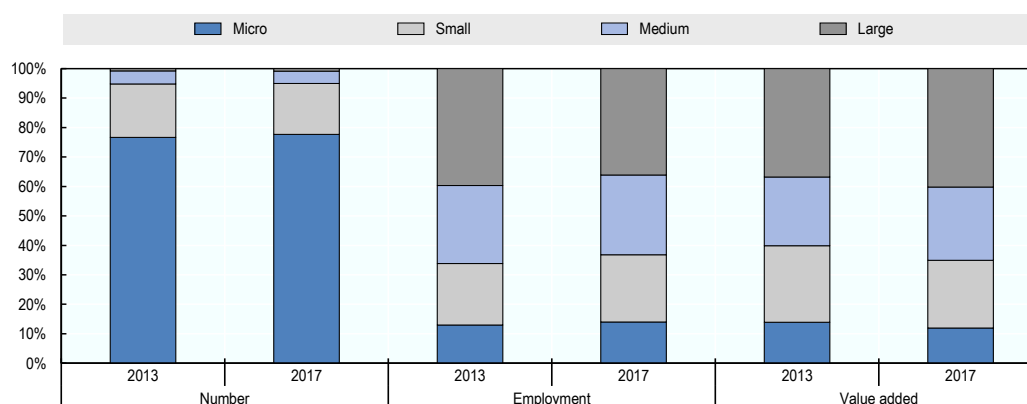
	EU definition	Law on Enterprises
Micro	< 10 employees ≤ EUR 2 million turnover or balance sheet	No definition in place
Small	< 50 employees ≤ EUR 10 million turnover or balance sheet	< 50 employees < BAM 2.8 million (~EUR 1.43 million) turnover < BAM 1.4 million (~EUR 0.71 million) circulating assets
Medium-sized	< 250 employees ≤ EUR 50 million turnover ≤ EUR 43 million balance sheet	< 250 employees < BAM 4 million (~EUR 2.04 million) turnover ≤ BAM 8 million (~EUR 4.08 million) circulating assets

Note: BAM: Bosnia and Herzegovina convertible mark; exchange rate as of December 2018.

Sources: Brčko District (2011^[24]), *Zakon o preduzećima Brčko distrikta BiH: prečišćen tekst (Law on enterprises Brčko District of BiH (consolidated text))*, www.secbdbih.org/files/legislativa/zakoni/ba/64_sjednica_zakon_o_preduzecima_bd_bih_preciscen.pdf.

Like its regional peers, Bosnia and Herzegovina's economy is dominated by SMEs. In 2017 there were around 30 000 SMEs (99.1% of all businesses) operating in BiH, with a large majority (77.7%) being micro enterprises. Small and medium-sized firms constituted slightly more than 20% of all SMEs. As Figure 14.2 shows, SMEs create much more employment than large enterprises. Even though their contribution to overall business sector employment has fallen by 4.4% since the last assessment, they still provided around 64% of jobs in the business sector 2017. At the same time, on average, SMEs contributed 60% to the annual value added in the business sector, which is around the regional average.

The share of businesses owned by women in Bosnia and Herzegovina is not known, as the statistical agencies in Bosnia and Herzegovina do not collect data on this indicator as part of their structural business statistics.

Figure 14.2. Business demography indicators in Bosnia and Herzegovina (2013 and 2017)

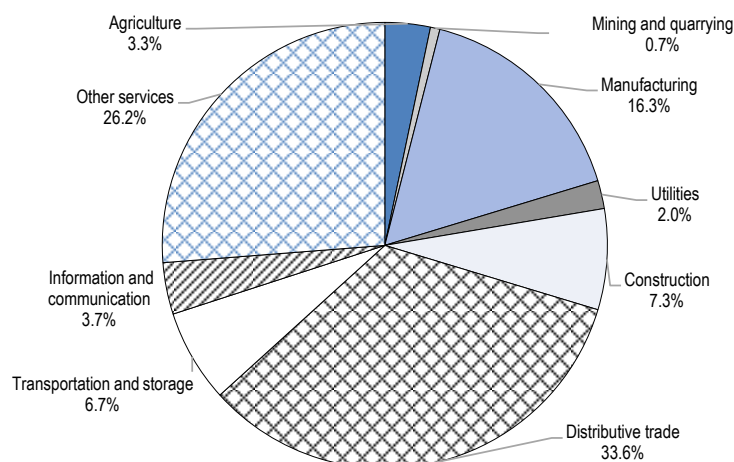
Note: Data do not include unincorporated enterprises. Due to the unavailability of state-level data, data for Bosnia and Herzegovina have been calculated by aggregating the data of the Federation of Bosnia and Herzegovina and the Republika Srpska.

Source: Statistical offices of FBiH and the RS.

StatLink  <http://dx.doi.org/10.1787/888933937850>

When it comes to the sectoral distribution of SMEs in Bosnia and Herzegovina, distributive trade was the largest sector for SMEs, accounting for one-third of active SMEs in 2017 (Figure 14.3). It was followed by the manufacturing sector, which accounted for 16.3% of SMEs (down from 19% in 2016). Transportation and storage accounted for 6.7%, similar to construction (7.3%).

Figure 14.3. Sectoral distribution of SMEs in Bosnia and Herzegovina (2017)



Note: Due to the unavailability of 2017 state-level data, figures for Bosnia and Herzegovina have been calculated by aggregating the data of the Federation of Bosnia and Herzegovina and the Republika Srpska. The sector classification generally follows the Statistical Classification of Economic Activities in the European Community (NACE) Rev.2 classification of productive economic activities with the following exceptions: “Utilities” represents the sum of “Electricity, gas, steam and air conditioning supply” (D) and “Water supply, sewerage, waste management and remediation activities” (E); “Distributive Trade” covers “Wholesale and retail trade; repair of motor vehicles and motorcycles” (F); and Other Services here consists of (I) Accommodation and food service activities, (L) Real estate activities, (M) Professional, scientific and technical activities, (N) Administrative and support service activities as well as (S) Other service activities. For more information, consult NACE Rev. 2 Classification.

Source: Statistical offices of FBiH and the RS.

In 2017 more than 70% of SMEs were located in the FBiH, with around 30% in the RS (Table 14.6). In the FBiH, SMEs were primarily concentrated in and around the main commercial hubs, and in particular around Sarajevo (23% in 2017).

Table 14.6. Number of registered companies in Bosnia and Herzegovina, by enterprise size and entity and FBiH canton (2017)

Entities	Cantons (FBiH)	Enterprise size, by employment				Total	Share of total number of enterprises
		0-9	10-49	50-249	250+		
Federation of Bosnia and Herzegovina ¹	Bosnian Podrinje	112	58	14	3	187	0.57%
	Herzegovina-Neretva	1 686	675	174	24	2 559	7.86%
	Canton 10	457	164	27	2	650	2.00%
	Posavina	233	111	25	3	372	1.14%
	Canton Sarajevo	5 078	1 884	487	98	7 547	23.18%
	Central Bosnia	1 137	496	155	30	1 818	5.58%
	Tuzla Canton	2 425	1 042	312	36	3 815	11.72%
	Una-Sena	1 299	535	118	8	1 960	6.02%
	West Herzegovina	763	365	97	23	1 248	3.83%
	Zenica-Doboj	1 642	833	243	39	2 757	8.47%
	Total FBiH	14 832	6 163	1 652	266	22 913	70.4%
Republika Srpska²		7 434	1 711	400	100	9 645	29.6%
Bosnia and Herzegovina		22 226	7 874	2 052	366	32 558	100%

Note: Data for the FBiH are collected from the Federal Information Agency and slightly differ from those obtained from the Statistical office of FBiH, reported in the main text.

Sources: ¹ Federal Information Agency; ² SBA assessment government questionnaire.

Assessment and recommendations

Process

The Small Business Act (SBA) assessment cycle was launched in Bosnia and Herzegovina with a kick-off meeting in Sarajevo on 8 November 2017. The meeting was organised in co-operation with the Ministry of Foreign Trade and Economic Relations, which acts as the SBA Co-ordinator, nominated by the European Commission, and which is responsible for implementing the SBA principles.⁴

During the meeting, the new assessment framework (see Policy Framework and Assessment Process chapter for details) was presented to the line ministries and public institutions at all government levels, and contribution to the information collection process was requested. The two documents making up the assessment framework – the questionnaire and statistical data sheet – were explained in depth to the participants, directing particular attention to the newly added questions and indicators.

Following the launch event, the Ministry of Foreign Trade and Economic Relations distributed the questionnaire to the appropriate counterparts in the ministries and government agencies at the state level, and sent the statistical sheet to the National Statistical Office of BiH. In parallel, the questionnaire and the statistical sheet were also shared with the entity representatives: in the FBiH, the Ministry of Development, Entrepreneurship and Craft; and in the RS the Ministry of Industry, Energy and Mining. These representatives distributed it to their counterparts in the relevant ministries and agencies. From November 2017 to February 2018, the necessary data and documentation were compiled, subsequent to which the questionnaire was completed. In so doing, a score for each policy dimension was assigned, accompanied by a justification. The completed questionnaires and statistical data sheets were sent to the OECD team on 5 February 2018.

The review of the inputs by the OECD and the partner institutions revealed the need for additional information on certain elements. This was requested from the state Ministry of Foreign Trade and Economic Relations; the Ministry of Development, Entrepreneurship and Craft of the FBiH; and the Ministry of Industry, Energy and Mining of the RS. The updated questionnaire was revised, and sent back to the OECD on 29 March 2018.

Meanwhile, an independent assessment was also conducted by the OECD and its partner organisations. This was based on inputs from a team of local independent experts in Bosnia and Herzegovina who collected data and information, and conducted interviews with key public and civil society stakeholders, as well as with SME representatives.

Following the completion of the government self-assessment and independent assessment, two reconciliation meetings were organised by the OECD and the European Bank for Reconstruction and Development (EBRD) in Banja Luka and Sarajevo on 5 and 6 June 2018, respectively. The meetings aimed to close any remaining information gaps in the questionnaire, while also serving as an opportunity to seek the views of a broad range of policy stakeholders on how SMEs are affected by current policies, and what else can be done across different policy areas to improve SMEs' performance and competitiveness in Bosnia and Herzegovina. For the two policy dimensions whose assessment was led by the European Training Foundation (entrepreneurial learning and women's entrepreneurship, and enterprise skills), similar meetings took place in Sarajevo on 13 and 14 March 2018.

The reconciliation meeting allowed the assessment findings to be consolidated. The OECD and partner organisations decided on the final scores under each policy dimension presented in this report (more information on how the scores are calculated can be found in Annex A and Annex B). The preliminary findings and scores were subsequently presented to SBA Co-ordinators at a meeting in Paris on 12 July 2018. The draft SME Policy Index publications and the SBA Assessment profile of Bosnia and Herzegovina were made available to the government of BiH for their review and feedback during August-November 2018.

Scoring approach

Each policy dimension and its constituent parts are assigned a numerical score ranging from 1 to 5 according to the level of policy development and implementation, so that performance can be compared across economies and over time. Level 1 is the weakest and Level 5 the strongest, indicating a level of development commensurate with OECD good practice (Table 14.7).

For further details on the SME Policy Index methodology and how the scores are calculated, as well as the changes in the last assessment cycle, please refer to Annex A.

Table 14.7. Description of score levels

Level 5	Level 4 plus results of monitoring and evaluation inform policy framework design and implementation
Level 4	Level 3 plus evidence of a concrete record of effective policy implementation.
Level 3	A solid framework, addressing the policy area concerned, is in place and officially adopted.
Level 2	A draft or pilot framework exists, with some signs of government activity to address the policy area concerned.
Level 1	No framework (e.g. law, institution) exists to address the policy topic concerned.

Entrepreneurial learning and women's entrepreneurship (Dimension 1)

With scores of 3.23 for entrepreneurial learning and 3.26 for women's entrepreneurship, BiH has improved on both sub-dimensions since the 2016 assessment (Figure 14.1), and is placed around the regional average for this policy dimension (Table 14.8). There have been some good policy developments, particularly on entrepreneurial learning, but the challenge now is translating policy into concrete actions. This will require all schools to be supported, and teachers prepared, to deliver on the entrepreneurial learning agenda. Policy on women's entrepreneurship has also improved since 2016, but more co-ordination involving all the competent authorities, as well as exchange of good practice and know-how, would help the wider women's entrepreneurship ecosystem. The inclusion of women's entrepreneurship within the wider economic policy landscape remains weak.

Table 14.8. Scores for Dimension 1: Entrepreneurial learning and women's entrepreneurship

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 1: Entrepreneurial learning and women's entrepreneurship	Sub-dimension 1.1: Entrepreneurial learning	Planning and design	4.13	3.73
		Implementation	2.65	3.61
		Monitoring and evaluation	3.33	2.57
		Weighted average	3.23	3.43
	Sub-dimension 1.2: Women's entrepreneurship	Planning and design	3.67	3.57
		Implementation	3.29	3.16
		Monitoring and evaluation	2.60	2.37
		Weighted average	3.26	3.12
	BiH's overall score for Dimension 1		3.24	3.31

State of play and key developments

Entrepreneurial learning

Since the 2016 SBA assessment there has been renewed momentum on entrepreneurial learning, particularly around plans to co-work the entrepreneurship key competence with digital competence developments. This represents an important policy step for BiH and was a direct response to feedback from the European Commission on the country's 2018-20 Economic Reform Programme (ERP), including the most recent EU policy recommendations (Council of the European Union, 2018^[25]) and support tools for both competences (Bacigalupo et al., 2016^[26]; Carretero, Vuorikari and Punie, 2018^[27]). This renewed interest reinforces BiH's commitment to develop the entrepreneurship key competence laid out in the BiH Strategic Framework (BiH Council of Ministers Directorate for Economic Planning, 2015^[28]) and the 2017-19 ERP (BiH, 2017^[29]). While policy interest in these two competences has been particularly prompted by EU policy developments, further progress will require a more concerted domestic commitment, and stronger mechanisms for policy co-operation and co-ordination among the education systems.

The 2016 SBA assessment highlighted that an important achievement was the creation of a common core curriculum which included the entrepreneurship key competence. In 2017, a state-wide dialogue involving policy makers and pedagogic institutes was initiated to consider how to implement a system-based response to a revised EU key competence policy, including the 2016 European Entrepreneurship Competence Framework. BiH now needs a framework implementation plan. This should include the structures and capacity required for monitoring and evaluation, and should also set out the role of schools, pedagogic institutes, education agencies and ministries in that process. The implementation plan's activities should build on the expertise, experience and materials developed through pilot actions acquired through an earlier EU-supported programme, including initiatives developed independently of international aid. One example of good practice is the small grants facility of the Federal Ministry of Education and Science which supports entrepreneurship – this acts as an incentive to schools to self-develop and innovate. Further developments on pedagogic approaches for entrepreneurial learning should prioritise “learning by doing” (EC, 2013^[30]).

Teacher training remains an important priority, but there has been little development in this area since the 2016 assessment. A state-wide entrepreneurship key competence implementation plan should encompass universities which provide pre-service teacher training programmes, and build on the existing capacity of the pedagogic institutes.

Entrepreneurship promotion in higher education has received little strategic attention since the last SBA assessment, and there has been little policy interest in how the higher education community addresses the entrepreneurship key competence. However, the efforts of Tuzla University to provide entrepreneurship courses outside the economics faculty is good practice. With business centres at the universities of Banja Luka, Mostar and Sarajevo providing support to students in building business plans and start-up activities, BiH should examine the opportunities to connect these activities and expertise within universities for developing smart specialisation.⁵

Women's entrepreneurship

Since the 2016 assessment, an informal working group supported by Gesellschaft für Internationale Zusammenarbeit (GIZ) and chaired by the Ministry of Foreign Trade and Economic Relations ensures dialogue and co-ordination on women's entrepreneurship developments among policy makers from all entities, including business and civic interest groups. As it is donor-supported, the sustainability of this group and its advisory potential needs to be assured, however. In the meantime, consideration should be given to developing a more comprehensive policy position on women's entrepreneurship, beyond the sole focus on entrepreneurship support for women in rural areas as laid out in the BiH Strategic Framework (BiH Council of Ministers Directorate for Economic Planning, 2015^[28]).

At entity level, the Council for Women's Entrepreneurship in the Republika Srpska demonstrates the leadership role of the Chamber of Commerce in prioritising women's entrepreneurship through policy engagement, training and international networking. The council provides important institutional support for women's entrepreneurship as part of the government's SME strategy, and oversees the implementation of a dedicated women's entrepreneurship development programme. The RS Government has also adopted a Women's Entrepreneurship Development Strategy for the period 2018-22.

In the FBiH, a women's entrepreneurship strategy development working group led by the Federal Ministry for Development, Entrepreneurship and Crafts (FMRPO) provides the

basis for a more established advisory body on women's entrepreneurship. Grants to support women-owned businesses at cantonal level (e.g. in Sarajevo, Tuzla) are good practice. Meanwhile, the drafting of a women's entrepreneurship action plan by the Brčko District is an opportunity to raise the profile of women's entrepreneurship policy and activities. All entities, including the informal working group led by the Ministry of Foreign Trade and Economic Relations, need to pay more attention to monitoring and evaluating women's entrepreneurship activities.

In line with previous SBA assessments, non-government organisations (NGOs) continue to play an important role in supporting women's entrepreneurship. The BiH Association of Women Entrepreneurs and the Women's Entrepreneurship Council in the RS (through a dedicated portal) provide information on financial support, training, good practice and networking opportunities. MI BOSPO – a micro-credit foundation – is an important player in supporting women's access to finance.

The way forward for Dimension 1

Policy interest in all the entities in promoting a more entrepreneurial culture through education and training is an important factor in BiH developments. Plans to update a state-wide strategy on entrepreneurial learning, including a more strategic approach to developing the entrepreneurship key competence, align well with wider policy at EU level. The challenge is to ensure that this policy interest is translated into an action plan and that this is implemented.

For women's entrepreneurship, while there are good policy efforts and a support framework primarily focused on "necessity" entrepreneurship (defined primarily in terms of social inclusion), more policy attention is needed on "opportunity" entrepreneurship (defined in terms of competitiveness) – in particular, how policy and support measures can boost the growth and innovation potential of women's businesses.

Moving forward, the following actions should be considered

- **Update the entrepreneurial learning strategy.** In line with constitutional competences, the strategy on entrepreneurial learning should be updated and accompanied by a framework implementation plan drawing on the European Entrepreneurship Competence Framework (EntreComp) and including capacity building of ministries and pedagogic institutes in system-based monitoring and evaluation. School-business co-operation should be given a higher priority. The strategy should also include development of financial literacy – which is as a key component of EntreComp – and link with the wider financial literacy strategy recommended below (see Dimension 6). The implications of entrepreneurial learning for careers guidance and counselling should also be considered. Current discussions to co-work entrepreneurship competence development with digital competences should be followed up with a concrete plan and then implemented.
- **Embed women's entrepreneurship within economic reform plans.** Women's business development, including training, strategic networking and financial support, should be integrated within the wider economic reform plans at all levels. This will require more systematic gender-specific data on SME support and monitoring.

Bankruptcy and second chance for SMEs (Dimension 2)

Bosnia and Herzegovina has improved its performance in this dimension, from a score of 2.25 in 2016 (Figure 14.1) to 2.55 in this assessment (Table 14.9).

Table 14.9. Scores for Dimension 2: Bankruptcy and second chance

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 2: Bankruptcy and second chance	Sub-dimension 2.1: Preventive measures		1.14	2.39
	Sub-dimension 2.2: Bankruptcy procedures	Design and implementation	3.25	3.71
		Performance, monitoring and evaluation	2.45	2.46
		Weighted average	2.93	3.21
	Sub-dimension 2.3: Promoting second chance		1.94	1.93
BiH's overall score for Dimension 2			2.55	2.87

State of play and key developments

Preventive measures and bankruptcy procedures

The legislative framework for bankruptcy proceedings in Bosnia and Herzegovina is regulated at the entity level. The Federation of Bosnia and Herzegovina, the Republika Srpska and the Brčko District each have their own legal frameworks regulating bankruptcies. Nevertheless, the entities are making efforts to harmonise their legislation on bankruptcy proceedings.

In the FBiH, bankruptcy proceedings are governed by the Law on Bankruptcy Proceedings⁶ last amended in 2006 and 2017, and the Law on Liquidation Proceedings,⁷ enacted in 2003. In 2016, the Constitutional Court of the FBiH froze all bankruptcy proceedings as two articles (33 and 40⁸ of the Law on Bankruptcy Proceedings) were considered unconstitutional. Consequently, a new amendment in line with the RS's bankruptcy law was presented to the FBiH Parliament in 2017, and adopted in 2018.⁹

In the RS, a new Law on Bankruptcy¹⁰ was adopted in 2016. The law is compatible with the European Commission recommendation of March 2014 on a new approach to business failure and insolvency (EC, 2014_[31]). The new law sets out objectives such as the timely initiation of bankruptcy proceedings, and the financial and operational restructuring of the debtor. Accordingly, it allows a non-liquid company to enter into a settlement with creditors and if there are delays in the process sanctions can be introduced against bankruptcy trustees.

In the Brčko District, the Law on Bankruptcy, Compulsory Settlement and Liquidation¹¹ enacted in 2002 governs bankruptcy proceedings. The law sets out the conditions for the implementation of bankruptcy proceedings, compulsory settlement and liquidation against the debtor.

According to their laws on bankruptcy proceedings, the key players in insolvency proceedings in the FBiH and the RS are the insolvency courts, the insolvency judges, the bankruptcy trustees and the creditors (acting through an assembly of creditors and the creditors' committee).

In both entities, bankruptcy proceedings may be initiated by the bankruptcy debtor or any creditor under the conditions provided by the law. Debtors are considered insolvent if they cannot settle their financial obligations within 60 days. In the FBiH, the petition must be filed within 30 days, while in the RS it is 60 days.

In the FBiH, the law does not provide for the possibility of a pre-bankruptcy settlement before filing for bankruptcy. By contrast, the new law adopted in the RS offers the possibility of a pre-bankruptcy settlement before filing for bankruptcy. In 2017 in the RS a total of 11 restructuring cases were initiated, and 4 firms have already completed restructuring, saving 600 jobs (IFC, 2018_[32]). In both entities, if a debt restructuring settlement cannot be agreed between debtor and creditors, the process ends in liquidation.

The legislation covers all aspects of secured transactions in Bosnia and Herzegovina, including the ability of secured creditors to satisfy their secured claim as well as their right to be paid first out of the proceeds from the sale of the assets in which they have collateral. The creditors of a lower payment rank only have their claims paid following the full payment of the superior rank. Creditors from the same rank have their claims paid *pro rata*.

According to the new law in the RS, bankruptcy procedures should be resolved within one year, and in extreme cases two years. The legal frameworks of the FBiH and the Brčko District do not stipulate any time limit for resolving insolvency. On average, in 2018 it took 3.3 years to resolve an insolvency case in Bosnia and Herzegovina, the second longest in the WBT region after Turkey (World Bank, 2018_[14]).

In 2018, insolvency procedures cost 9% of the debtor's estate. The average recovery rate for creditors has increased from 37.3 cents in 2016 to 38.9 cents on each dollar owed in 2018, but it is still far below the OECD average of 69.83 cents.

The Central Registry of Credits, which operates under the co-ordination of the Central Bank of Bosnia and Herzegovina, collects data on all debts related to legal entities and natural persons which have been recorded by commercial banks, microcredit institutions, saving-credit institutions and leasing companies. The information on the registry is only accessible upon the written approval of the businesses so there are no mechanisms for using these data to identify potentially distressed or distressed companies.

Data on bankruptcies are only collected in the Republika Srpska (Table 14.10).

Table 14.10. Number of bankrupt enterprises per year in the Republika Srpska (2013-16)

	2013	2014	2015	2016
Number of bankrupt enterprises	113	103	128	115

Source: Government of the Republika Srpska (2017).

Promoting second chance

Bosnia and Herzegovina has no special measures that discriminate against entrepreneurs who have failed to restart their business. In the Republika Srpska natural or legal persons cannot establish a company or participate in the share of another company until they have settled their debts (e.g. social security contributions) in the register of fines, a measure primarily aimed at protecting workers' rights. There are no initiatives to promote second chance among entrepreneurs in the FBiH or the Brčko District. However, in the RS Strategy for the Development of SMEs 2016-2020, the second strategic objective for the

business environment is “faster implementation of bankruptcy proceedings and providing a second chance for entrepreneurs”. The action plan states that seminars will be organised during 2016-20 to promote “second chance” among entrepreneurs, though there are no additional details and at the time of writing, no activities had been carried out in that area. Danube Chance 2.0, launched in October 2018 in the RS under the co-ordination of the Republic Agency for the Development of Small and Medium-Sized Enterprises (RARS), aims to develop second chance policies for entrepreneurs, as well as practical solutions to improve entrepreneurial learning and culture to avoid the loss of entrepreneurial potential and overcome the stigmatisation of entrepreneurs who have gone bankrupt (Center for Social Innovation, 2018^[33]).¹²

The way forward for Dimension 2

Bosnia and Herzegovina can further improve its legal framework for bankruptcy and second chance policies in the following ways:

- **Continue to harmonise the insolvency legal framework with the European Commission recommendation.** Formulating the legal framework which delimits the market entrance and exit rules for businesses is a core government role. First, it is crucial to adapt the legislative framework to the natural evolution of the business environment, as has occurred in Slovenia (Box 14.2) and second adopting similar rules among different entities will reduce the administrative burden for distressed companies. Therefore, the Federation of Bosnia and Herzegovina needs to adapt its legal framework to the needs of the economy.
- **Enhance and adapt the administrative capacities** of the bodies implementing the new insolvency practices in the framework: bankruptcy administrators, bankruptcy judges, appraisers and creditors’ associations. The economy should consider offering training and limited-duration licensing for implementation bodies to ensure better quality services. Constant monitoring and auditing of their work should mean they meet higher professional standards and ensure they maintain high-quality services.
- **Create a monitoring and evaluation process for bankruptcy mechanisms.** Proper monitoring and evaluation leads to evidence-based policy making, and consequently can enhance the policy expectations of businesses.
- **Develop a fully fledged early warning system:** SME owners have a tendency to underestimate their financial difficulties and to resist taking action to alleviate their hardships. Therefore, Bosnia and Herzegovina should consider introducing a system which would convince entrepreneurs to initiate recovery measures without delay. Such a system could take different forms, but should entail certain essential features. First, special detection procedures should be devised that would screen and monitor early signs of SMEs in financial difficulties. Second, those SMEs identified need to be approached and provided with advice on objectively assessing their financial situation, as well as on the different options available to them concerning recovery. Once they are better informed, SMEs would be able to take the required steps at an earlier stage, thereby increasing their chance of survival. Early warning mechanisms established by EU member states can offer a blueprint for Bosnia and Herzegovina (Box 14.3).

Box 14.2. Slovenia: A post-crisis insolvency regime

Having joined the EU in 2004, Slovenia adopted a new insolvency law in 2007. However, this coincided with the financial crisis and the newly introduced regulations were not enough to deal with the high number of non-performing loans and failed entrepreneurs. The previous regulations were found to be one of the main causes of creditors' low recovery rates (EBRD, 2014^[34]). To improve the situation, the Slovenian government amended the insolvency law in 2013. The main changes included:

- a new pre-insolvency restructuring procedure
- mechanisms to facilitate restructuring.

The restructuring mechanisms included debt-equity swaps, giving priority to restructuring plans proposed by major creditors, and giving shareholders control of business operations. The new system is based on compulsory settlement, simplified compulsory settlement (solely for micro and small enterprises and individual entrepreneurs), pre-insolvency restructuring proceedings, and bankruptcy.

This reform quickly began to have a positive impact on Slovenia's business environment. Within two years of its adoption, the percentage of companies using one or more of the procedures doubled, rising to almost 15% of cases in 2015. Furthermore, the recovery rate of secured creditors increased from 50.1 cents on the dollar in 2013 to 88.2 cents in 2015. The level of entrepreneurship and company formation also increased, having a clear impact on the SME ecosystem in general.

These changes also brought the Slovenian insolvency regime in line with best international practice, with the economy joining the trend of facilitating debt/equity swaps in order to conduct debt restructuring (IMF, 2015^[35]).

Sources: EBRD (2014^[34]), *Commercial Laws of Slovenia: An Assessment by the EBRD*, www.ebrd.com/documents/legal-reform/slovenia-country-law-assessment.pdf; IMF (2015^[35]), "Republic of Slovenia: Selected issues", www.imf.org/external/pubs/ft/scr/2015/cr1542.pdf; <https://www.imf.org/external/pubs/ft/scr/2015/cr1542.pdf> World Bank (2017^[36]), *Doing Business 2018: Reforming to Create Jobs*, www.doingbusiness.org/en/reports/global-reports/doing-business-2018.

Box 14.3. Early Warning Europe

The international project Early Warning Europe (EWE) was developed with the objective of promoting SMEs' growth across Europe by assisting them during financially difficult periods. In 2016, Early Warning Europe applied for funding through Europe's Competitiveness of Enterprises and Small and Medium-Sized Enterprises (COSME) programme and obtained almost EUR 5 million. The first wave of the project ran for three years and focused on setting up a full-scale early warning mechanism in Poland, Italy, Greece and Spain.

The consortium is comprised of 15 partners in 7 countries including mentor partners Early Warning Denmark, TEAM U in Germany, Dyzo in Belgium, authority partners such as the Danish Business Authority, the regional government of Madrid and the Polish Agency for Enterprise Development, as well as EU-level associations such as the, European Small

Business Alliance, Eurochambres and SME United. The Early Warning Europe project is financed by COSME and aims to provide assistance to businesses and entrepreneurs in trouble, as well as those who wish to better anticipate problems. The project builds new best practice and draws on existing experience from these 15 organisations. Currently, five new EU Member States are in the process of joining the EWE community, and several others have expressed their interest. EWE is open to all COSME countries, and the expansion in phases gives access to the early warning mechanisms foreseen in the upcoming EU Directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures.

The consortium is composed of three groups of organisations: 1) mentor organisations with substantial experience in providing support to companies in distress; 2) national or regional organisations that intend to implement early warning mechanisms; and 3) organisations that are responsible for supporting the pan-European communication and dissemination activities of the project.

Through EWE, entrepreneurs can receive help from consultants to get a clear overview of the company, identify the areas which are causing problems, and propose further remedial activities. The second step of the restoration process is collaboration with a mentor. Mentors work closely with the entrepreneur providing expertise, knowledge and support to get the enterprise back on the right track. Alternatively, they can guide companies toward a quick, organised closure when this is the best option for the company. This also contributes greatly to the company owner's chances of a second start and reduces the loss for the owner, the creditors and society as a whole.

Independent evaluations show a highly positive impact on society of the Early Warning system in terms of jobs saved and savings for the public treasuries. Evaluations show a general saving of 20% for the public treasuries on company closures under the Early Warning mechanism, a high level of job preservation and significantly better first-year turnover and growth after the Early Warning intervention.

An innovative element of the project is the introduction of artificial intelligence and the processing of big data in detecting early signs of distress in companies. Early Warning Europe has developed a data model that identifies the probability of distress in companies in Poland, Italy, Greece and Spain based on publicly accessible data, allowing the network partners to proactively assist companies that may not otherwise realise their problems before it is too late.

Currently the project has the support of more than 500 mentors. The support provided is impartial, confidential and free-of-charge. In the first wave, EWE provided support to 3 500 companies in distress in Poland, Spain, Italy and Greece. In its second wave (2017-19) the project will support the establishment of early warning mechanisms in five additional EU Member States, with the ultimate goal of establishing early warning mechanisms in all EU Member States.

Source: Early Warning Europe (2018^[37]), *Early Warning Europe website*, www.earlywarningeurope.eu/.

Institutional and regulatory framework for SME policy making (Dimension 3)

With a score of 2.62, Bosnia and Herzegovina is the lowest performer in this dimension in the WBT. However, its score has improved since 2016 (when it was 2.22, see Figure 14.1). This is mainly due to some progress at the state level on regulatory impact analysis (RIA) and public-private consultations (PPCs), as well as some developments at the entity level, principally in the Republika Srpska, in each of the three sub-dimensions (Table 14.11).

Table 14.11. Scores for Dimension 3: Institutional and regulatory framework for SME policy making

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 3: Institutional and regulatory framework for SME policy making	Sub-dimension 3.1: Institutional framework	Planning and design	2.79	4.06
		Implementation	3.09	4.06
		Monitoring and evaluation	2.94	3.92
		Weighted average	2.97	4.03
	Sub-dimension 3.2: Legislative simplification and regulatory impact analysis	Planning and design	2.24	4.00
		Implementation	2.10	3.25
		Monitoring and evaluation	1.71	3.23
		Weighted average	2.06	3.47
	Sub-dimension 3.3: Public-private consultations (PPCs)	Frequency and transparency of PPCs	2.84	3.86
		Private sector involvement in PPCs	3.09	4.26
		Monitoring and evaluation	1.67	2.73
		Weighted average	2.71	3.79
	BiH's overall score for Dimension 3		2.62	3.79

State of play and key developments

Institutional framework

Bosnia and Herzegovina's institutional framework for SME policies is still underdeveloped at the state level. In fact, SME policies only exist at the entity level. As noted in the previous assessment, there is still a lack of vertical co-ordination and linkages to help align SME policy objectives across the entities, and policy co-ordination remains weak.

In the RS, the key SME policy document is the Strategy for the Development of SMEs 2016-2020 (the SME strategy). The strategy was adopted in September 2016 and contains clear and measurable targets and measures, complemented by a detailed action plan. As in the previous cycle, the Department for SMEs in the Ministry of Industry, Energy and Mining is responsible for policy development and co-ordination, while the implementation of the SME strategy is carried out in partnership with RARS. The SME strategy has not always been implemented consistently, since an over-reliance on donor funds causes occasional delays and impedes the full realisation of the planned activities.

The FBiH has neither an SME strategy nor a public agency to co-ordinate SME policy implementation or SME-related activities. As in the previous assessment, it has only one

strategic document for fostering entrepreneurship – the Development of Small and Medium-sized Enterprises in the FBiH 2009-2018 and its related action plan for 2016-18. This regulates the SME environment indirectly. The institution indirectly in charge of SME-related issues is the Federal Ministry for Development, Entrepreneurship and Crafts (FMRPO). The Economic Reform Programme of Bosnia and Herzegovina 2017-19 envisages establishing an SME development agency in the FBiH in 2018 (BiH, 2018^[10]). However, this has not yet happened.

None of the entity-level strategic documents include measures to combat the informal economy – nor are there any concrete plans and actions at the state level. In the RS, the informal economy is being indirectly addressed through the reform of the fiscal system, which is reducing administrative and parafiscal burdens on businesses through the new Law on Tax System and amendments to the Law on Income Tax, adopted in 2017 and 2018 respectively.

As in the previous assessment, SME-related strategic documents are regularly monitored at the entity level. In addition to this, the work of RARS in the RS is also regularly tracked and annual reports are produced. This assessment found some new initiatives to evaluate SME policies in the RS. For example, in September 2016 the Council for SME Development and Entrepreneurship was established as the government advisory body mandated to monitor and evaluate SME policies and their impact on the ground.

Legislative simplification and regulatory impact analysis

Legislative simplification is being undertaken at the entity level and their implementation record is successful, especially in the RS where a regulatory guillotine has been continuously in use. Since its launch in 2009, it has eliminated 25% of unnecessary formal procedures for businesses and 60% of redundant inspection procedures. In the FBiH over the same period, the application of a regulatory guillotine has led to the simplification of business permits (65% of the total number identified for simplification) and to significant savings for the private sector. In 2016, the FBiH adopted a new law on enterprises which aimed to simplify the procedures for starting a business (for more information see Section Operational environment for SMEs (Dimension 4)). However, since the last assessment, the intensity of the reviews and simplification efforts has decreased in BiH.

In July 2017, the Unified Rules for Legal Drafting were amended to formally introduce RIA into the policy development process at the state level. The SME test is not embedded into the RIA, however. According to the Unified Rules many institutions are responsible for providing opinions on RIA according to their area of expertise, co-ordinated by the General Secretariat of the Council of Ministers of BiH. For instance, the Ministry of Finance and Treasury is in charge of providing opinions on the fiscal impact identified by the institution proposing a new law, and the Ministry of Foreign Trade and Economic Relations is supposed to provide opinions on the economic and environmental impact identified. Despite these developments, RIA is not yet implemented at the state level.

Requirements to conduct RIA have been rooted in the policy-making systems of both the FBiH (since 2014) and the RS (since 2015). Both entities provide clear and comprehensive RIA guidelines, which include examples of RIA files, and are available on line (OECD, 2017^[38]). The General Secretariat (GS) of the government is the institution responsible for RIA in the FBiH and the Ministry of Economic Relations and Regional Co-operation (MERRC) in the RS. The annual reports produced by GS and MERRC show that the quality of the RIA process is not satisfactory. In particular, only

27% of draft laws in the FBiH were actually supported by RIA or another type of analysis. The main challenges in the FBiH are a lack of planning of the RIA process, the limited involvement of the GS in the RIA development process and the absence of proper enforcement mechanisms that would enable the GS to return low-quality RIA reports to the drafting ministry (OECD, 2017^[38]). The latter is also an issue in the RS, where the MERRC also has no formal right to return RIAs of low quality to the originating ministry. On a positive note, the RS administration did produce RIAs for all regulations stipulated by law. However, these were mostly “short RIAs”, which offered only limited policy analysis (OECD, 2017^[38]).

Public-private consultations

As in the previous assessment, all three levels of government in BiH have legal and regulatory frameworks in place that define the general principles and procedures for the conduct of public-private consultations (PPCs). In 2017, the state and the Brčko District amended and adopted their respective rules concerning PPCs (OECD, 2017^[38]). In practice, PPCs are assessed as being poor and inconsistent (with some signs of improvement in the RS). The evidence shows that the majority of laws in BiH are adopted through an urgent procedure, without consulting interested parties. In 2016, 58% of legislation was adopted in this manner (OECD, 2017^[38]).

Since the last assessment, BiH has continued its efforts to improve the transparency of its public-private consultations. In particular, in 2016 the state level introduced a centralised e-consultation portal¹³ listing all the PPCs that concern institutions at the state level. The number of institutions using the e-consultation portal increased from 25 in 2016 to 37 in 2017 and 39 in 2018 (Council of Ministers, 2018^[39]). The efficiency and effectiveness of the portal, however, are not regularly monitored or evaluated.

As was found in the previous SBA assessment, SMEs are only partially involved in PPCs at all government levels. With the exception of the RS, participation is only possible in most cases by invitation. The private sector is mostly represented through business associations.

Monitoring of PPCs is carried out regularly at the state level and in the RS. At the state level, the Ministry of Justice is entrusted with monitoring PPCs, and issues a report every two years on the implementation of the Rules of Consultations in legislative drafting. Its 2017 report highlighted that the quality of online PPCs at the state level needed to be improved, since the e-portal was not consistently used by the relevant institutions. It also noted that the public were not providing sufficient comments on the available legislative drafts (Ministry of Justice, 2018^[40]). In 2017, 13 out of 23 online legislative proposals received no feedback (Ministry of Justice, 2018^[40]). Therefore, it seems that the public are either not aware of the e-portal or are uninterested in taking part in consultations.

Overall, there are no quality checks on the process, as there is no central unit responsible for examining whether PPCs are conducted on time and if the feedback and concerns of SMEs have been taken into consideration.

The way forward for Dimension 3

Despite making some progress in this dimension, Bosnia and Herzegovina needs to further improve its institutional and regulatory framework. Some of the most pressing actions to take are:

- **Establish effective co-ordination of SME policy across the different levels of government.** The state institutional framework for SME policies is still underdeveloped, with SME policies only existing at entity level (in the RS in particular) in accordance with the constitutional setting of BiH. It is essential to establish a state-wide institutional framework, i.e. an SME development strategy for BiH that would forge SME policy synergies across the various government levels and act as an appropriate basis for SME policy development in BiH. During this process, it will be important to establish vertical co-ordination and linkages to help align SME policy objectives between the entities.
- **Ensure full implementation of RIA, including aspects affecting SMEs.** The requirement for RIA was introduced at the state level in 2017, but it has not yet been implemented. There are several reasons for this: there are no clear RIA guidelines with concrete examples of RIA files, officials are not trained to conduct RIAs and there is an overall lack of awareness of the benefits of RIA as a regulatory policy tool. The government should therefore provide RIA training to government officials and distribute clear guidelines with concrete examples on how to conduct RIAs. The government could also use the Council of Ministers (CoM) to ensure the quality of RIAs by giving it a clear mandate to return RIA documents deemed to be below par to the responsible institution for revision before the proposal goes to the government. The same practice could be adopted at the entity level as well.
- **Enhance the quality of the PPC process and ensure SMEs can participate effectively.** BiH should consider introducing a central co-ordination unit within the Ministry of Justice or the CoM to supervise the use of the single government portal for consultations and act as a quality control mechanism for PPCs. It is also important to promote PPCs and (re)create trust in consultations through greater transparency by publishing reports on PPCs, highlighting which proposals were accepted and which were not, and why. SMEs could be encouraged to participate more in discussions on business-related legislation in BiH. The example of Montenegro's Business Caravan could be a model for the government (Box 14.4).

Box 14.4. Reaching out to SMEs to develop a more favourable business environment: Montenegro's Business Caravan

Preparations for the new MSME Development Strategy in Montenegro started with a "Business Caravan" in March 2017. The Business Caravan was a set of meetings with private sector representatives, organised by the Ministry of Economy in co-operation with the United Nations Development Programme (UNDP), which aimed to gather SMEs' insights into the quality of the current SME support programmes and government measures. Over the course of 15 months, the government (led by the Minister of Economy herself) held meetings with private sector representatives in 14 Montenegrin municipalities to discuss SME policies' strong and weak points and potential avenues for improvement.

One of the main catalysts for the caravan was SMEs' weak participation in support programmes and public-private consultations in general. The Business Caravan is a mechanism to reach out to SMEs and contact them directly. Local SMEs were contacted through local municipality offices and the SME response to these meetings was substantial. The presence of the minister in the meetings added weight to discussions and encouraged active participation by entrepreneurs, who shared their opinions, suggestions

and observations.

The SMEs' feedback was collected methodically and analysed by experts from the Ministry of Economy, which took the lead in drafting the new SME development strategy. It produced a report with an overview of the suggestions that were accepted and included in the strategy, as well as those that were not, with a clear explanation for the decision.

Sources: Data provided by the Government of Montenegro as part of the SBA Assessment; Vijesti (2017^[41]), Babić: *Biznis karavan daje rezultate* [Babic: *Business Caravan Gives Results*], www.vijesti.me/vijesti/babic-biznis-karavan-daje-rezultate-949619.

Operational environment for SMEs (Dimension 4)

Bosnia and Herzegovina have the lowest score in the region for this dimension (2.34), indicating that it has much room to improve the operational environment for SMEs (Table 14.12). However, some steps are now being taken to simplify the operational environment for SMEs; their impact will be more visible in the next assessment period.

Table 14.12. Scores for Dimension 4: Operational environment for SMEs

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 4: Operational environment for SMEs	Sub-dimension 4.1: Digital government services for enterprises	Planning and design	2.25	4.07
		Implementation	1.97	3.47
		Monitoring and evaluation	1.00	2.05
		Weighted average	1.81	3.29
	Sub-dimension 4.2: Company registration	Design and implementation	3.90	4.48
		Performance	2.28	3.72
		Monitoring and evaluation	1.91	3.59
		Weighted average	2.78	3.97
	Sub-dimension 4.3: Business licensing	Licence procedures	3.70	3.67
		Monitoring and streamlining of licence system	3.32	3.18
		Weighted average	3.51	3.43
	Sub-dimension 4.4: Tax compliance procedures for SMEs	SME tax compliance and simplification procedures	No scores	
		Monitoring and evaluation of SME-specific tax measures		
BiH's overall score for Dimension 4			2.34	3.45

Note: A new sub-dimension 4.4 on tax compliance procedures for SMEs was added at the request of the assessed economies, to better reflect the complexity of the overall picture of the operational environment for SMEs, however, as it is a pilot analysis this sub-dimension has not been included in the scoring.

State of play and key developments

Digital government services for enterprises

The fragmentation of responsibilities among authorities at different levels has a direct impact on e-government services. It creates a dual barrier to the provision of e-services, with no centralised portal to provide them and no central co-ordination body to oversee the services offered across Bosnia and Herzegovina.

In addition, the Public Administration Strategy 2018-22 announced by the Council of Ministers has not yet been adopted, meaning the economy has not had a strategic public administration framework since the end of 2014. A similar situation applies to the legal framework. The Law on the Information Society Agency covering various aspects of digital government as part of the EU *acquis* has not been adopted either.

Despite some progress since 2016 in the digitalisation of basic services, such as online tax filing and e-cadastre registry, the level of implementation differs in both entities. This is mainly due to the different approaches adopted. While the FBiH relies exclusively on the laws adopted at the state level, the RS has its own laws and strategic frameworks.

Since the last assessment, the Law on Electronic Signature¹⁴ and the Law on Electronic Document¹⁵ have been adopted, but their implementation is still ongoing in the RS. The

Office for Supervision and Accreditation within the BiH Ministry of Communication and Transport only started to function as of January 2018. Accordingly, the e-IDs introduced to support the full use of electronic identification and e-signatures cannot be used due to different interpretations and implementation of the legal framework at different administrative levels, despite the creation of a national accreditation body. In order to create an accreditation authority, the RS is currently establishing the National Digital Identity Management Center of Republic of Srpska, expected to be operational in 2019.

Another positive concrete development is the electronic submission of tax forms through the Tax Administration, which has become possible in both entities since the previous assessment. In the FBiH online filing is limited to salaries and contributions, annual income tax and property tax. The RS has implemented the mandatory electronic filing of applications for tax refunds since January 2017 as part as one of the specific objectives of its Tax Administration Strategy 2016-18.

Electronic cadastre has been established at the entity level. The Federal Bureau for Geodetic and Property Legal Affairs manages the e-cadastre in the FBiH (www.katastar.ba/pocetna.aspx). In the RS, the e-cadastre is managed by the Department of Geodetic and Property Affairs (www.ezkrs.net). However, e-cadastrs are only available for viewing data; SMEs and individuals have no way of obtaining official electronic documents from the real estate registry.

There is no substantial collaboration over data exchange among the public institutions of the different entities. However, a few institutions do have unified databases, such as the Taxation Office, Pension Fund, Healthcare Fund, Unemployment Office and Statistical Office. When it comes to interoperability, all entities have successfully implemented the project on Increasing the Capacity of the Inspection System in BiH, with the support of the World Bank. This platform will form the technical infrastructure of the interoperability structure and will enable the exchange of information among the RS, the FBiH, the Brčko and the institutions at the state level.

Bosnia and Herzegovina has been a member of the Open Government Partnership since 2014. However, it has not developed an action plan, despite members being required to do so. Moreover, there are no initiatives in either the RS or the FBiH to monitor and evaluate digital services.

Business registration and licensing

Each entity is responsible for its own business registration process. In the Republika Srpska, the entire procedure is conducted by the Agency for Intermediary, IT and Financial Services (APIF). It acts as a one-stop shop, with all the necessary registration and notification procedures handled through one place. The FBiH's one-stop shop is not yet operational but it is expected to be so by the end of 2019. It will cover all 54 municipalities, and aims to handle all processes through single location. In the Brčko District, business registration can only take place in the Brčko District Court of Bosnia and Herzegovina.

The registration process provides two company numbers: 1) the registration number, which is specific to the entity; and 2) the state-level value-added tax (VAT) number. However, a registration is not valid for the entire economy: a company registered in the FBiH, for example, cannot operate directly in the RS without obtaining additional permits, and vice versa.

Electronic company registration is being developed in the RS and should be up and running by the end of 2018. Currently, APIF's website (<https://www.apif.net>) and the RS Chamber of Commerce and Industry's website (<http://komorars.ba/poslovnio-kruzenje/normativni-okvir/privredno-sistemske-oblasti/privredna-drustva/>) provide entrepreneurs with access to all the relevant information and links to registration forms and manuals, making it easier to start a company. In the FBiH, registration can only be achieved in person, because the law on registration¹⁶ has not been amended to allow a legal basis for the establishment of online company registration.

Bosnia and Herzegovina remains the outlier among the WBT economies for the cost and length of time involved in starting a business, requiring 13 procedures and 81 days to start a business. The cost of starting a business has increased from 13.5% of income per capita in the 2016 assessment to 14.9% (World Bank, 2018^[14]).

Obtaining licences and permits remains a complex and fragmented process for SMEs in Bosnia and Herzegovina. Licences are obtained at the entity level from a number of public institutions. Each institution at the entity level is responsible for providing licences and permits according to their competences. Business licences for SMEs are defined under the Law on Companies of the FBiH and the RS. However, for craftsmen, licences are processed at the municipality or city level.

Both entities provide publicly available written information on the procedure for obtaining business licences. However, according to the interviews with private sector representatives, applicants in the FBiH have to seek professional assistance to get detailed information or else have to check the law by themselves. In the RS, the situation is much better. Applicants can get information on all licences and permits from the newly established (2018) Registry of Authorizations/Approval (<https://pscsrpska.vladars.net/sr>), which is the single point of contact for businesses, co-ordinated by the MERRC of the RS.

In terms of streamlining licence systems, since 2014, SMEs in the RS have been able to apply for a licence or make changes to an existing company licence at a single office. However, no centralised procedures exist in the FBiH or at the state level and there is no central co-ordination body to oversee licences granted across the entire territory.

Tax compliance procedures for SMEs

Bosnia and Herzegovina offers a presumptive tax regime for micro businesses, administered at the state level for indirect taxes (VAT) and at the entity level for direct taxes. In accordance with the Law on Value-Added Tax,¹⁷ enterprises with an annual turnover below BAM 50 000 (EUR 25 500) are not obliged to register in the VAT system in the entire territory.

Only businesses operating in the RS are able to benefit from lower income tax rates. In accordance with the Law on Income Tax in the RS,¹⁸ unincorporated businesses¹⁹ with an annual income of less than BAM 50 000 (around EUR 25 500) are granted an income tax rate of 2%, with a minimum payment of BAM 600 (around EUR 300), instead of the standard rate of 10%.

In the FBiH, some taxpayers are able to pay lump-sum income tax if they meet one of the following criteria: 1) sole proprietorship and performing artisanal activities; 2) traditional crafts established by the Decree on the Protection of Traditional and Old Crafts, and with a maximum of two employees; 3) transport activities (up to 8 tonnes); or 4) agricultural or forestry activities as a basic occupation, and not registered for VAT (see above). Neither

the Brčko District nor the FBiH have any additional tax compliance procedures for SMEs.

The way forward for Dimension 4

Bosnia and Herzegovina needs to further improve its operational environment for SMEs framework. The following points list a number of areas, requiring further attention by the policy-makers:

- **Create a single portal and expand digital services, allowing SMEs to complete all processes on line.** This will help the government and SMEs to have a clear overview of all the available e-services, saving time and reducing both the cost and the number of required procedures for SMEs.
- **Harmonise and continue efforts to implement digital authentication or e-signatures in order to allow SMEs to complete services fully on line and across the entire territory.** E-signatures or digital authentication allow users to complete all processes on line which saves time as the current system means they need to be physically present to complete services.
- **Harmonise the business registration process and widen online registration opportunities for SMEs.** This will allow SMEs to perform their activities over a wider geographical scope, saving time and lightening the administrative burden by reducing the number of steps required.
- **Pursue efforts to streamline company registration and licensing under one-stop shops.** A one-stop shop increases transparency, speeds-up processes, helps to conduct effective monitoring and streamlining, and lowers administrative burdens and costs for SMEs. This central unit can also play the role of a central co-ordination body, enhancing interoperability. Estonia's X-Road (Box 14.5) is a good practice example on how to overcome possible challenges in the early implementation phase of a central co-ordinating system rollout.
- **Regularly monitor and evaluate tax simplification measures.** Compliance with the eligibility criteria of simplified tax schemes in the region does not always remove complexity, as intended. Excessive documentation requirements coupled with the limited availability of online options to complete the procedures may deter entrepreneurs and SMEs from making use of these schemes. WBT governments should therefore evaluate how to facilitate compliance for SMEs under the tax simplification schemes, while maintaining sufficient safeguards that prevent abuse and result in low tax compliance.

Box 14.5. X-Road: Estonia's system for interoperable government service delivery and data exchange

The introduction of X-Road in Estonia in 2001 transformed its public service delivery. The system links up various public and private sector information systems, making secure data exchanges possible among public and private institutions. X-tee (as X-road based solution is called in Estonia) became the official data exchange layer for the state information system and the backbone of e-Estonia. Information that is stored in a server can be shared with institutions that request it for their service provision.

X-Road connects relevant bodies including the tax and customs board, population and

company registers, several commercial banks and many more. X-Road increases the transparency of the public service delivery, as data exchanged through X-Road are authenticated using Estonia's e-ID system and can be traced to their origin or even used as evidence in courts of law (Cybernetica, 2018^[42]). It also offers better opportunities to monitor existing services and reduces the risks associated with data storage because no single server holds all the information. It is, instead, held across several servers.

The Estonian Government passed the Public Information Act in 2000, and the use of X Road was made mandatory in 2003. Today, X Road connects more than 600 institutions and enterprises, and approximately 52 000 organisations are indirect users of the more than 2 700 services that can be used via X-Road. Based on its usage figures, it is estimated that every year, X-Road saves more than 800 years of working time.

Many factors have made X-Road particularly successful. It was developed in the early 1990s in a post-Soviet Union context, so there was almost no legacy framework in place. At that time Estonia was one of the first countries to adopt an e-government strategy. Political will and citizens' desire to break with the Soviet era and establish a new government system created a unique opportunity. However, Estonia quickly realised that legislation had to be adjusted to ensure integrity. Estonia's Public Information Act prohibits the establishment of separate databases for the collection of the same data. In practice, it means that state institutions cannot repetitively ask for the same personal information if it is already stored in any of the data repositories connected to X-Road.

Source: (Vassil, 2015) X-Road (2018^[43]), *Factsheet*, www.ria.ee/x-tee/fact/#eng.

Support services for SMEs (Dimension 5a)

Since the last assessment in 2016, Bosnia and Herzegovina has improved its performance in this policy dimension, with an increase of its overall score from 2.42 to 3.41 (Figure 14.1). The improvement in its overall score reflects improvements made in both sub-dimensions. However, BiH still falls short of reaching the WBT average score in both sub-dimensions.

Table 14.13. Scores for Dimension 5a: Support services for SMEs

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 5a: Business support services for SMEs	Sub-dimension 5a.1: Business support services provided by the government	Planning and design	3.07	3.84
		Implementation	3.26	3.68
		Monitoring and evaluation	2.12	3.19
		Weighted average	2.98	3.63
	Sub-dimension 5a.2: Government initiatives to stimulate private business support services	Planning and design	4.43	4.67
		Implementation	3.64	3.85
		Monitoring and evaluation	3.50	4.07
		Weighted average	3.85	4.14
	BiH's overall score for Dimension 5a:		3.41	3.89

State of play and key developments

In Bosnia and Herzegovina, business support systems (BSSs) are designed and implemented at the entity level. SMEs which want to benefit from a BSS programme provided by the relevant public institutions in one of the entities need to be registered in that entity. The FBiH and the RS both have strategy documents with accompanying action plans that include actions to improve BSS provision to SMEs. The Brčko District, however, does not possess a SME-specific strategy document and nor do its public institutions provide BSSs to SMEs, with the exception of co-financing support to SMEs for certification with an upper support limit of BAM 10 000 (around EUR 5 100) per SME per year.

In the Federation of Bosnia and Herzegovina, the 2016-18 action plan as part of the strategy document Development of Small and Medium Enterprises in the Federation of Bosnia and Herzegovina 2009-2018 includes measurable targets for the relevant actions. For example, it expects to improve the visibility of BSSs through promotional events and the media to inform more SMEs about available services. The action plan sets a target of a 10% increase in SMEs applying for BSSs delivered by the FMRPO by 2018. In the Republika Srpska, the action plan of the 2016-20 SME Strategy includes dedicated actions to improve BSS provision. However, although these actions are associated with monitoring indicators, they do not include measurable targets. For example, the action plan foresees RARS establishing a mentoring system. This action is associated with monitoring indicators such as “trained mentors” or “supported SMEs”, but it does not specify how many mentors should be trained or how many SMEs supported by 2020.

In the RS, RARS is the dedicated public institution in charge of BSS provision to SMEs. In 2017, it had a total budget of almost BAM 5.9 million (around EUR 3 million). RARS provides information on how to register a business, and periodically delivers one-day training courses on how to develop a business plan. It co-ordinates the 14 local development agencies which have been established across the Republika Srpska, as well

as SMEs' engagement with the Enterprise Europe Network. RARS has also implemented a number of projects which were supported by international donors, such as the support programme for innovative SMEs in co-operation with the Swedish International Development Cooperation Agency. The FBiH has no entity-level public agency to provide training or mentoring to SMEs. This function is carried out by the Federal Ministry of Development, Entrepreneurship and Crafts and regional development agencies in some cantons. While the FMRPO does not directly deliver training to SMEs, it provides information on relevant legislation and offers co-financing schemes.

An important development in this assessment period, which will improve BSS provision in the future, has been Bosnia and Herzegovina's participation in the second phase of the Establishment and Promotion of Mentoring Service for SMEs in the Western Balkans project. This project, which is being implemented in co-operation with the Japan International Cooperation Agency (JICA), seeks to build up a mentoring system provided to SMEs through development agencies in Serbia, Bosnia and Herzegovina, Montenegro and North Macedonia. The project follows the business support methodology developed by Serbia's former National Agency for Regional Development in co-operation with JICA and proposes the same programme activities. In Serbia, where the programme was standardised in 2008, it achieved very positive results (see Box 14.6).

In the FBiH, the programme is implemented by regional development agencies such as the Sarajevo Economic Region Development Agency (SERDA); 16 mentors were trained at SERDA and about 100 SMEs benefitted from its mentoring support over the three years between 2013 and 2016 (SERDA, 2018^[15]). In 2017, SERDA implemented this mentoring programme with support from the European Fund for South East Europe – it benefitted 30 SMEs from the Sarajevo Canton and Eastern Sarajevo. In 2018, the FMRPO trained 17 new mentors in co-operation with SERDA. The FMRPO publishes on its website calls for participation by SMEs in this free-of-charge mentoring programme. In the RS, RARS is in the process of training future mentors.

Box 14.6. The Development Agency of Serbia's standardised mentoring service

Background

The Development Agency of Serbia's (RAS) mentoring programme is designed to provide timely, continuous mentoring support to SMEs and start-ups with growth potential at crucial stages of their business paths. The programme began in 2005, using a business support methodology developed by the National Agency for Regional Development in co-operation with JICA. In 2008, following a three-year pilot period that saw positive results, RAS standardised the programme and has run it ever since.

Programme activities

The mentoring programme follows a sequence of four main steps: 1) diagnosis; 2) analysis and action plan (proposing measures to improve the business); 3) intervention (implementing the proposed measures); and 4) evaluation and tracking.

The programme allocates an expert mentor to spend a certain number of hours (from 25 to 50 hours per beneficiary) at the beneficiary's premises. The mentor and the SME's director jointly conduct a diagnosis to understand the business's operations, the reasons for any current problems or obstacles to further development, and the areas with the growth potential. Based on the factors identified, the mentor and the beneficiary then

prepare a plan/development project. The business support plan could potentially relate to any functional area of the enterprise, including organisational structure, human resources management, financial management, logistics and distribution, production-technological processes, intellectual property, and quality systems. Depending on need, the mentor could also refer the SME to more specialised consulting services.

Impact

- 2005-06: 37 civil servants received certified training by JICA
- 2006-09: more than 700 businesses supported
- 2011-12: 268 SMEs supported
- 2013-14: 213 SMEs supported
- 2015-16: 204 SMEs supported
- 2017: 253 SMEs supported

Results and feedback from SMEs (up to 2015)

- 99% of beneficiaries completed the entire programme
- 92% of beneficiaries felt there was a positive impact on some aspect of their business
- 95.2% of beneficiaries accepted almost all the proposed measures to improve their business.

It is also worth noting that the programme gave a significant number of RAS personnel the opportunity to upgrade their skills and knowledge. This professional development has had a positive impact on the RAS and, in turn, enabled the agency to provide long-term support to the national SMEs base via the same trained civil servants.

The programme also contributed to raising awareness among Serbian SMEs about the importance and benefits of expert advisory support and non-financial business support schemes.

Success factors

While the programme faced a number of challenges during its planning and implementation phase, caused by bureaucracy and systemic public sector delays, it nonetheless achieved all its objectives. Furthermore, its results were so positive that they led to the mentoring programme being institutionalised in 2011 as a standard service for SMEs in Serbia, delivered by the RAS with support from JICA.

Source: RAS (2017^[44]), *Create Life: Public Call for the Implementation of Standardised Mentoring Service*, <http://ras.gov.rs/en/sme-development/public-calls/create-life-public-call-for-the-implementation-of-standardised-mentoring-service>; information collected from RAS over the course of this assessment.

Over the course of this assessment period, SMEs in both the FBiH and the RS have had access to co-financing schemes.

In the RS, RARS provides co-financing for consultancy support within the Consultant Network programme, covering 50% of eligible costs with an upper support limit of BAM 3 000 (around EUR 1 500). The total amount allocated to this programme in 2018 was BAM 44 870 (around EUR 22 900). In the FBiH, the FMRPO provides co-financing of 50% of eligible costs to SMEs under the Strengthening the Competitiveness of SMEs programme. This covers three areas: 1) technological improvement, improvement of

product quality and standardisation of business and production processes; 2) training; and 3) market access and product promotion. In 2017, the total budget available for the first of these areas amounted to BAM 1.2 million (around EUR 610 000), of which BAM 250 000 was funded by the EU, with an upper support limit of BAM 38 000 (around EUR 19 400). The second area was allocated BAM 500 000 (around EUR 255 000), of which BAM 200 000 was financed by the EU, with an upper support limit of BAM 17 000. The third area has a budget of BAM 300 000 (around EUR 153 000) and an upper limit of BAM 10 000 (around EUR 5 100). Entrepreneurs under the age of 35 and women entrepreneurs have preferential access to this programme.

Both RARS and the FMRPO monitor their BSS provision, and compile annual monitoring reports. However, these reports are not publicly available (the latest financial audit report available on the RARS website dates back to 2015). In the FBiH, SMEs which benefitted from co-financing under the Strengthening the Competitiveness of SMEs programme need to report on the use of the grants, but are not asked to detail how satisfied they were with the scheme in general. Similarly, the RS has no formal mechanisms to collect the feedback of public BSS beneficiaries comprehensively and to use this information to adapt BSS provision accordingly.

RARS and the FMRPO provide information about BSSs on their websites. One notable development during this assessment period has been a joint project by RARS and the Ministry of Industry, Energy and Mining to establish a single web portal (www.preduzetnickiportalsrpske.net) for the RS in 2017. The project was financed by the European Union through the EBRD which also implemented it. The portal provides information on business practices, legislation and government institutions, associations, and international financial institutions such as the EBRD which are relevant to SMEs or which provide BSSs. It also features a database of private sector consultants, searchable by municipality, and their area and sector of expertise. This database is also available on the RARS website and at the time of writing featured 96 consultants. While the FMRPO does not provide a similar database, the Chamber of Economy of the Federation of Bosnia and Herzegovina does.

According to data received for this assessment, 387 SMEs benefitted from the FMRPO's BSSs in 2017 and 722 SMEs benefitted from publicly co-funded BSSs in the RS. This means that only 1.97% of SMEs in the FBiH, and 7.73% of SMEs in the RS used a publicly funded or co-financed BSS in 2017. In comparison, 23.1% of SMEs in Turkey and 18.8% of SMEs in Serbia used a publicly (co-)financed BSS, while the average for the seven WBT economies was 7.6% of SMEs.

The way forward for Dimension 5a

While Bosnia and Herzegovina has made progress over the course of this assessment period, it could consider the following actions to improve its BSS provision to SMEs:

- **Analyse the needs and supply of BSSs more effectively and regularly** to fill the gaps in BSS provision, better target the support provided and create more effective BSS provision systems. Over this assessment period, the relevant public institutions in the FBiH and the RS have not conducted a training needs analysis. They should make sure that BSS programmes and initiatives are tailored to the characteristics and dynamics of micro and SME beneficiaries, as well as to the industry sector they belong to, their stage of development and actual experience in the market. This should be done in co-operation with chambers of commerce or SME associations.

- **Strengthen the monitoring and evaluation of BSS programmes in both entities.** This is of paramount importance for increasing the effectiveness of BSSs and public budget allocation and spending. Both entities should also consider calling in an independent institution to conduct an in-depth evaluation of the BSSs offered by public institutions, assessing the impact of BSS programmes according to key performance indicators and avoiding overlap.
- **Introduce a quality assurance mechanism, such as an accreditation system for private sector consultants** which SMEs are required to use under co-financed support programmes. With the exception of the mentoring services provided through JICA, SMEs can freely choose a private sector consultant under either the FBiH's Strengthening Competitiveness of SMEs programme or the RS's Consultant Network programme. Both entities should consider introducing an accreditation system to ensure private sector providers have a minimum level of experience and qualifications. Subsequently, it could limit SME co-financing support to accredited private sector consultants and trainers.

Public procurement (Dimension 5b)

Bosnia and Herzegovina obtains a weighted score of 3.57 for this dimension (Table 14.14), the second worst result for the WBT economies. However, BiH was one of only three economies which has made progress since 2016, when it scored 2.3 (Figure 14.1), and has also achieved the biggest improvement in score. This progress was made from a very low starting level, though.

Table 14.14. Scores for Dimension 5b: Public procurement

Dimension	Thematic block	BiH	WBT average
Dimension 5b: Public procurement	Policy and regulatory framework	2.89	3.92
	Implementation	4.28	4.05
	Monitoring and evaluation	2.85	3.24
	Weighted average		
BiH's overall score for Dimension 5b		3.57	3.84

State of play and key developments

There have been no changes to public procurement provisions during the assessment period. Public procurement is regulated under the Public Procurement Law of 2014 (the PPL). The PPL is based on the EU Public Procurement Directives adopted in 2004; the 2014 EU Procurement Directives are yet to be implemented. Comprehensive amendments to the PPL to transpose these directives are in progress, and the draft of the relevant law was finalised by a working group in July 2018.

The general principles of the PPL are that contracting authorities should act transparently, and treat candidates or bidders equally, without discrimination and in a manner that will ensure active competition. The aim is to ensure the most efficient spending of public funds, taking into account the subject matter of procurement and its purpose. Foreign companies have access to contracts awarded in Bosnia and Herzegovina, but the PPL provides for the mandatory application of preferences for domestic bidders, which are regulated in a special implementing regulation adopted by the Council of Ministers. For the purposes of comparison and selection of the best tender, the prices submitted by domestic bidders are calculated in accordance with a preference factor of 10% for procurement procedures conducted in the period 2017-18 and of 5% until the end of 2019. Only companies from Central European Free Trade Agreement (CEFTA) countries are ensured equal treatment as domestic companies.

Apart from domestic preferences, there are not as many barriers and limitations in access to public procurement as elsewhere in the region, such as limitations concerning subcontracting or special requirements for consortia. PPL provisions allow for all the instruments which are relevant for enabling SMEs to access public procurement procedures: the division of procurement into lots, joint bidding (participation of consortia), subcontracting, and the application of proportionate and non-discriminatory requirements concerning the participation of economic operators.

Although the PPL allows contracting authorities to divide public procurement contracts into lots, they are not obliged to do so. When contracting authorities do divide the subject matter of procurement into lots, all the lots must be marked in the bidding documentation so as to allow the bidders to submit bids for one lot, several lots or all the lots. The contracting authorities should clearly and precisely define in the bidding documentation

the conditions and manner of submission of bids for lots. The public procurement contract should be concluded separately for each lot but if one bidder is successful on two or more lots, a single contract may be concluded. Contracting authorities may also limit the number of lots for which bidders may apply for. In this case they should reject the tenders of bidders who submitted tenders for more lots than they were allowed. In practice, 25-40% of procurement procedures are divided into lots.

Strategic documents related to public procurement now pay more attention to the issue of the participation of SMEs. The Public Procurement Strategy emphasises the need to pay particular attention to SMEs' situation when preparing amendments to the PPL, and defines those elements which would improve the participation of SMEs in public procurement procedures in Bosnia and Herzegovina.

The Public Procurement Agency (PPA) is an independent administrative body responsible for policy making, preparing draft legislation, monitoring, and advisory and training activities in the field of public procurement. It has two branch offices, in Banja Luka and Mostar. The PPA submits a report to the government every year on the functioning of the public procurement system. However, it does not apparently collect and analyse information about the obstacles encountered by SMEs in accessing public procurement; nor do the annual reports provide information about the participation of SMEs in public procurement procedures. However, they do include rich statistical data on the contracts awarded and the origin of economic operators who won the contracts. For example, according to the 2017 report, domestic suppliers obtained 98.6% of all concluded contracts in 2016. The annual report for 2016 also showed an increase in the value of contracts awarded to groups of economic operators: they represented 12.5% of the value of all awarded contracts, up from 4.9% in 2015. Groups of economic operators still only obtained a small number of public contracts, however: 0.18% of all concluded contracts in 2016, up from 0.17% in 2015.

The Procurement Review Body (PRB) is an independent and autonomous institution responsible for reviewing complaints submitted by economic operators. Any economic operator with or having had an interest in a public procurement contract award is allowed to appeal if they can make the case that damage was or could have been caused by the public procurement procedure because of the actions of the contracting authority. Before a complaint is submitted to the PRB, it should be examined by the contracting authority in question. Those appealing need to pay a fee before the appeal will be reviewed by the PRB. The fees are set according to the value of the entire public procurement contract and range from BAM 500 (around EUR 255) to BAM 25 000 (around EUR 12 800). In terms of the number of members, the PRB is the largest in the region, with 17 members. Besides its central office, the PRB has two branch offices in Mostar and Banja Luka which are responsible for reviewing appeals on smaller value procurement contracts. The branch offices do not have support staff, and the institution as a whole lacks basic technical resources, such as a website and professional e-mail addresses. Such shortages of supporting staff and technical resources have negative repercussions for the efficiency and quality of the overall functioning of the institution, especially in light of an increasing number of complaints.

The way forward for Dimension 5b

The biggest challenge for Bosnia and Herzegovina will be transposing and implementing the 2014 EU Public Procurement Directives. BiH should also improve its monitoring by increasing the range of information about public procurement which is collected and

processed by the PPA. It could do more to improve the access of economic operators to review procedures: the fees required to submit an appeal to the PRB are higher than in other economies of the region. On the positive side, Bosnia and Herzegovina has quite well-developed electronic public procurement instruments.

Going forward Bosnia and Herzegovina should put more emphasis on the following:

- **Further align national legislation with EU rules and international good practice.**
- **Ensure that economic operators have access to public procurement on equal footing regardless of their origin:**
 - Complete the implementation of 2014 EU public procurement directives.
 - Ensure that the PRB has a more prominent Internet presence, in particular its own website, where all the relevant information about appeals can be found alongside information about the PRB and the remedies and rulings it has adopted.
- **Remedy the issue of lack of expert staff in the PRB.**
- **Constantly monitor and analyse obstacles faced by SMEs in access to public procurement markets**, including the cost of access to legal protection in public procurement.
- **Lower the fees to be paid by economic operators** complaining to the PRB against the decisions of contracting authorities.

Access to finance for SMEs (Dimension 6)

With an overall score of 3.26 (Table 14.15), Bosnia and Herzegovina is now the worst performer of the seven WBT economies in this dimension, just behind Albania and Kosovo. While BiH has made tangible efforts to improve access to finance for SMEs, such as inter-entity aligning of banking regulation and strengthening non-bank finance regulation, SMEs' access to finance remains restricted by a fragmented administrative system and a lack of sustainable and evaluated support.

Table 14.15. Scores for Dimension 6: Access to finance

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 6: Access to finance for SMEs	Sub-dimension 6.1: Legal and regulatory framework	Creditor rights	3.85	4.20
		Registers	4.50	4.58
		Credit information bureaus	4.25	4.55
		Banking regulations	3.00	3.79
		Stock market	3.07	2.93
		Weighted average	3.87	4.14
	Sub-dimension 6.2 Bank financing	Banking lending practices and conditions	2.74	2.92
		Credit guarantee schemes	2.17	2.30
		Weighted average	2.51	2.67
	Sub-dimension 6.3: Non-bank financing	Microfinance institutions	4.33	3.57
		Leasing	2.75	2.84
		Factoring	1.75	2.45
		Weighted average	2.94	2.95
	Sub-dimension 6.4: Venture capital ecosystem	Legal framework	1.82	2.32
		Design and implementation of government activities	1.34	2.48
		Monitoring and evaluation	1.00	1.48
		Weighted average	1.44	2.22
	Sub-dimension 6.5: Financial literacy	Planning, design and implementation	1.38	2.44
		Monitoring and evaluation	1.00	1.19
		Weighted average	1.31	2.19
	BiH's overall score for Dimension 6		3.26	3.53

State of play and key developments

Legal and regulatory framework

The legal framework for secured creditors is well regulated across Bosnia and Herzegovina, with jurisdiction split between the entity and national levels. In 2016, the RS passed a new Bankruptcy Law, with support from the International Finance Corporation, which has further aligned proceedings with international best practice. While recovery rates and costs as percentage of estate are comparable to or better than regional averages, the process remains burdensome and lengthy (World Bank, 2018^[45]).

Banking regulation in Bosnia and Herzegovina falls under the entities' banking supervisory authorities. This area has seen particular improvement during the assessment period as both entities have passed new banking laws, strengthening supervision and

inter-entity alignment. These laws have brought the banking regulations further in line with the Basel II (and to some extent Basel III) requirements, particularly the new minimum capital adequacy ratio introduced in the RS in January and the FBiH in April 2018. While these regulations will require further fine-tuning with regards to countercyclical buffers and systemic bank buffers, this represents an important step forward.

The two entities also administer separate cadastres that together provide full coverage and are both accessible on line, much like the registration system for movable assets which is under national jurisdiction. A public credit information system is also in place, falling under the authority of the national government. There is also an operational national private credit information system, but it is neither recognised nor overseen by a regulator.

Both entities have had capital markets available since 2001 through the Sarajevo and Banja Luka stock exchanges, although neither offers a separate market for low capitalisation firms. In a positive move for market integration, both stock exchanges joined the EBRD-supported SEE Link in 2017, the regional platform for cross-market trading.

Sources of external finance for SMEs (bank financing, non-bank financing and venture capital)

Bank lending continues to be the dominant form of financing across Bosnia and Herzegovina. At 53% of GDP in 2016 it is substantially above the Western Balkan average of 45%. While there are no official numbers on lending to SMEs as a share of total lending, this is estimated at 48% (IMF, 2016^[46]; World Bank, 2018^[1]). According to data from the Central Bank of Bosnia and Herzegovina, the latest macroeconomic indicators are similarly favourable, with a notable increase in credit growth (7.2% year-on-year in 2017), supported by a reduction in non-performing loans from 15% of all loans in 2013 to 10% at the end of 2017 – highlighting the increased stability of the banking sector.

Government financial support schemes for SMEs are limited. There are support programmes for SMEs across the country, but complex administrative structures inhibit many aspects of their operation, from standardised data collection to the co-ordination of delivery mechanisms. For example, credit guarantee schemes in the FBiH are administered at an additional level of administration between the cantons and the entity, with no strategy, monitoring or evaluation at any higher administrative level – neither entity nor state. This means the credit guarantee schemes that SMEs have access to in the FBiH vary widely in size and terms depending on their location, and there are no reliable statistics on their uptake. The RS Government has a centralised credit guarantee scheme (through the RS Guarantee Fund), but uptake has fallen sharply – from EUR 1.8 million in 2015 to EUR 440 000 in 2016 – for reasons that remain unclear. Both entities provide publicly funded lending to SMEs, painting a very similar picture. In the RS, the Investment and Development Bank (IRBRS) provides only specialised loans (credit lines) through financial intermediaries from its own funds. Since 2015, the IRBRS has offered no direct loans to SMEs. In the FBiH, public sector lending is provided at cantonal level with no known involvement by the entity or state. The interest rate subsidies provided by some of the cantons also raise questions about sustainability, as they risk crowding out the private sector.

When it comes to non-bank financing, recent legislative changes have laid the groundwork for the expansion of these sources of finance. There are 12 microfinance

institutions in both entities, mainly self-funding with limited donor involvement. Leasing is available and well regulated across both entities following established best practices (recently amended in the FBiH), while dedicated factoring legislation was introduced in the FBiH with the 2016 Law on Factoring. Despite these positive legal developments, it is difficult to assess the actual uptake of these instruments in the absence of any state-level statistics. Only the RS makes any data on the uptake of non-bank financing available, and this shows an increase in microfinance and a decrease in leasing levels (reportedly due to high fees). No such information has been provided by the FBiH or a national body and it remains unclear to what extent it is collected.

The ecosystem to support the establishment of venture capital operations remains rudimentary. While both entities allow venture capital operations under their respective laws on investment funds, neither has a dedicated framework, nor any plans to establish one. RARS in the RS has prepared a study on venture capital regulation and risk capital activity, although any possible further steps and legislative or regulatory follow-ups remain unclear. Similarly, there are no business angel networks operating in Bosnia and Herzegovina, despite previous (donor-funded) attempts to create them. There are reports of tentative plans at the national level, but nothing specific has materialised.

Financial literacy

Mechanisms to support financial literacy in BiH show some promising signs, although overall implementation is hindered by the lack of a centralised strategy, monitoring or evaluation either at the entity or national level. Most notably, the secondary school curriculum of the Republika Srpska covers financial literacy and the education system provides training for teachers, though the exact scope remains unclear.

In the area of adult learning for either potential or existing entrepreneurs, the picture is similar to the rest of the Western Balkan region: scattered training targeting very particular groups without any prior needs assessment, centralised strategy, oversight or evaluation. At the national level, the donor-funded “U Plusu”²⁰ portal provides training and workshops across BiH, as well as online information, while in the RS, RARS the Chamber of Commerce and the ombudsman for the banking system implement ad-hoc training and awareness-raising events, as well as a central entrepreneurship portal.

The way forward for Dimension 6

While Bosnia and Herzegovina has shown signs of progress in some areas, several areas for further improvement remain:

- **Continue to align the financial space.** At the most fundamental level, SMEs’ access to finance remains inhibited by the complex administrative divisions and subsequent lack of policy alignment across the state. The ultimate aim of alignment should be to enable frictionless operation across the whole of Bosnia and Herzegovina – a single financial space – regardless of the level at which it is regulated. In this area, the recently strengthened co-ordination of banking supervision is a promising development. Similar initiatives in the field of support mechanisms, such as credit guarantee schemes, would go a long way towards simplifying the SME finance ecosystem.
- **Strengthen the non-bank financing ecosystem and standardise data collection.** Efforts should be made to standardise data collection for leasing and factoring to reliably capture the uptake of these increasingly important and (in the FBiH) newly

amended sources of alternative finance. Efforts to raise awareness of these alternative products could also help, especially where legal reforms are in place to facilitate higher uptake levels.

- **Introduce a financial literacy strategy.** Such a strategy, including standards and evaluation criteria for financial literacy training, would allow the stringent evaluation of all training and its subsequent adjustment, based on need.

Standards and technical regulations (Dimension 7)

Bosnia and Herzegovina's overall score for this dimension was already the lowest in the region in the 2016 assessment, and has fallen further, to 2.78 (Table 14.16). This is largely due to inadequate co-operation between the state and entity levels, leading to backlogs in aligning legislation with the EU *acquis*.

Table 14.16. Scores for Dimension 7: Standards and technical regulations

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 7: Standards and technical regulations	Sub-dimension 7.1: Overall co-ordination and general measures		1.83	3.12
	Sub-dimension 7.2: Harmonisation with the EU <i>acquis</i>	Technical regulations	2.47	3.87
		Standardisation	2.88	3.97
		Accreditation	2.44	4.53
		Conformity assessment	2.07	3.65
		Metrology	2.89	4.47
		Market surveillance	3.80	4.43
		Weighted average	3.09	4.15
		Sub-dimension 7.3: SME access to standardisation	Awareness raising and information	3.97
	SMEs participation in developing standards		1.00	2.57
	Financial support to SMEs		1.93	2.39
	Weighted average		2.30	3.07
	BiH's overall score for Dimension 7		2.78	3.83

State of play and key developments

Overall co-ordination and general measures

Bosnia and Herzegovina is yet to implement a mechanism for the overall co-ordination of its quality infrastructure pillars. The long-expected country-wide strategy on quality infrastructure was envisaged by the 2016-18 Work Programme of the Council of Ministers of BiH, but is yet to be adopted. The RS has established its own co-ordination body and has adopted a draft strategy for Quality Infrastructure of Products and Services for the period 2018-22. Where the entities have no mutually harmonised legislation, e.g. chemicals, food supplements and cosmetics, SMEs need to formally register in both entities to be able to place their products on the market and are audited by market surveillance authorities in each entity.

A designated portal and a contact point have not been established at the state level to assist SMEs in placing their products on the EU Single Market. In the RS, the Export Info Centre provides information on standards and technical regulations, and on how to comply with them, but SMEs in the FBiH can only access the relevant information from the websites of different ministries and government agencies.

Harmonisation with the EU *acquis*

The Law on Technical Requirement and Conformity Assessment mandates the BiH's Ministry of Foreign Trade and Economic Relations to issue technical regulations, based on the draft proposals of the BiH Committee for Technical Regulations. The committee,

composed of representatives from all levels of governments, led the transposition of seven New Approach directives.²¹ However, it has not convened since 2012 as the RS government first requested that the law be amended with respect to the committee's competences in issuing technical regulations and appointing conformity assessment bodies in BiH. Since then, EU legislation has not been aligned in a uniform manner throughout the economy. The RS continues to adopt legislation to transpose technical regulations separately from the state level, the FBiH and the Brčko District.

The Institute for Standardisation of Bosnia and Herzegovina (ISBiH) is the state body responsible for standardisation, including adopting international and national standards.²² In the RS, the Bureau for Standardisation and Metrology participates in the preparation of national standards but can also issue RS standards as entity standards. Currently, no RS standard has been issued and only national and international standards are in place. Co-operation between the two bodies in the area of standardisation is based on the 2011 Agreement of Co-operation. With only 38 employees out of the 52 originally planned, ISBiH only has enough staff to achieve the targets in its annual work plan, but cannot fulfill the need to translate European standards. As of August 2017, Bosnia and Herzegovina had adopted 20 093 European standards as national ones – an adoption rate of about 87%. Of these, 19 904 standards were adopted by the endorsement method, i.e. issuing an endorsement notice, which makes it difficult for SMEs to trace the relevant standards, understand their content or apply them correctly.

ISBiH is an affiliate member of the European Committee for Standardization (CEN) and the European Committee for Electrotechnical Standardization (CENELEC). One of the goals set by the strategy and action plan for the development of ISBiH for 2015-20 is to obtain full CEN/CENELEC membership. According to an internal evaluation of the respective action plan, it has already met 75% of the membership criteria. ISBiH is also a member of the International Organization for Standardization (ISO), and an associate member of the International Electrotechnical Commission.

In the area of accreditation and conformity assessment, state-level legislation is only partially aligned with the EU *acquis* and the RS develops and implements its own legislation in this area. The Institute for Accreditation of BiH (BATA) is responsible for implementing BiH's overall accreditation system. Its operations are in line with Regulation (EC) No.765/2008. In this area, the state legislation is applied throughout BiH and at all levels of government. All accredited CABs are easily accessible to SMEs through an online register on BATA's website, which provides detailed information on the type of activities they undertake.

Since 2015, BATA has had only 21 employees and is facing difficulties in supervising the increasing number of accredited bodies, which grew from 77 in 2016 to 116 in 2018.²³ In the immediate future, BATA expects to receive more applications for accreditation and will have additional tasks related to alignment with the EU *acquis*. Moreover, BATA aims to increase the formal recognition of its accreditations internationally. It is an associate member of the European Co-operation for Accreditation (EA) and signed a Bilateral Agreement (EA BLA) for calibration, testing (excluding medical laboratories) and inspection in 2012. BATA was positively assessed for these three fields in 2017 and according to its 2018-21 Medium-Term Action Plan, aims to extend the scope of the EA BLA with an additional field by 2021. BATA is also a full member of the International Laboratory Accreditation Co-operation and signatory to its Multilateral Recognition Agreement. Bosnia and Herzegovina has also established co-operation agreements in the area of accreditation with economies in the region. In October 2018, it signed a

memorandum of understanding (MoU) with Serbia to mutually recognise documents issued by accredited laboratories for industrial non-food products, which will further remove trade barriers and facilitate SME exports.

The current BiH legislation on metrology is not fully aligned with the EU *acquis*. The state-level Institute of Metrology of Bosnia and Herzegovina (IMBiH) is in charge of scientific metrology in Bosnia and Herzegovina, while legal metrology is conducted by IMBiH and two entity-level institutions (the Bureau of Metrology of the FBiH and the RS Bureau for Standardisation and Metrology). A Metrology Council has been established to better co-ordinate the work between the metrology institutions at the state and entity levels. However, its members are yet to be appointed due to disagreements between IMBiH and the entity-level institutions on the appointment procedure. In 2018, IMBiH significantly improved the metrology system by adopting 15 new rulebooks for measuring instruments. With 51 employees out of a planned 72, and a moratorium on hiring civil and non-civil servants in force since 2010, IMBiH is unable to further develop the metrology system in Bosnia and Herzegovina.

IMBiH is an associate member of the European Co-operation in Legal Metrology and a member of the European Association of National Metrology Institutes. It is also an associate state of the International Bureau of Weights and Measures, and a corresponding member of the International Organization of Legal Metrology. IMBiH has established co-operation with other national metrology bodies in the region. In 2017, it signed an MoU with Turkey's national metrology institute on co-operation in scientific and legal metrology. This co-operation includes joint research projects and developing legal metrology services for agriculture, the environment and medical devices in line with EU legislation.

Bosnia and Herzegovina's market surveillance system consists of the Market Surveillance Agency of BiH, and inspection authorities in the RS, the FBiH and the Brčko District. Co-operation among all these authorities is ensured through the National Co-ordination Board. According to the Market Surveillance Agency 2017's annual report, 20 product groups were treated as part of proactive surveillance and 27 cases were initiated through reactive surveillance. As a result of 190 product safety inspections, 7 263 unsafe products were withdrawn from the market and businesses have aligned 27 136 products with safety requirements. During this assessment period, the market surveillance authorities have emphasised guidance and support to local businesses. In 2016, the Market Surveillance Agency started publishing a guide for businesses with instructions on manufacturing and selling safe products. It is an annual publication with a focus on the products that will be subject to surveillance in the year of publication. In co-operation with BiH business associations, since 2017 the agency has organised four training and workshop events for businesses to support them in placing products on the EU and national markets.

SME access to standardisation

Bosnia and Herzegovina has only basic measures in place to facilitate SME access to standardisation. ISBiH publishes biannual information bulletins to inform the public about its activities and the latest developments from ISO and CEN/CENELC, but there are no practical guides on implementing standards or local case studies on the benefits of using them. Training to support SME implementation of standards and general awareness-raising events are rare. However, ISBiH has established a standardisation helpdesk for SMEs through its website.

Bosnia and Herzegovina is yet to introduce financial or other measures to encourage SME involvement in Technical Committees (TCs), such as covering their travel costs or introducing digital tools to ease their participation. However, participation in the work of the ISBiH expert bodies, including Technical Committees, remains free for SMEs and for all other interested parties. Committee meetings are also held in different cities to reduce the cost of participation for SMEs.

There are no financial support programmes at the state level. In 2017, the FBiH supported 12 SMEs to introduce international quality standards (HACCP, HALAL, introduction of CE marking), based on the annual Strengthening the Competitiveness of SMEs grant scheme. In the same year, 11 companies from the RS benefited from sector-specific grants (e.g. wood processing and textiles) provided in co-operation with the United States Agency for International Development's Workforce and Higher Access to Markets Activity (USAID WHAM) project. In the Brčko District, SMEs can benefit from subsidies to introduce international quality standards, based on the Brčko District Law on Subsidies from 2016.

The way forward for Dimension 7

The process of harmonising legislative framework with the EU *acquis* has stagnated in Bosnia and Herzegovina. In the future, policy makers should:

- **Develop a state-wide strategy on quality infrastructure and implement a co-ordination mechanism across different levels of government.** EU legislation is currently not being uniformly aligned throughout Bosnia and Herzegovina, leading to inadequate harmonisation not just with the EU *acquis*, but also between the entities. As a result, SMEs can have difficulties exporting to the Single Market and may be forced to register twice if selling their products in both entities. Given the limited institutional resources in both entities, co-operation will be important to further develop quality infrastructure system and support SMEs.
- **Improve SME access to standardisation.** Bosnia and Herzegovina should seek new channels to raise awareness of the benefits of standards among SMEs. Currently, ISBiH's awareness raising of standards is limited to biannual information bulletins and occasional public seminars. It needs to be more proactive to reach out to SMEs. It could offer sets of standards for particular sectors or disciplines and present them to SMEs during relevant events for their community, e.g. start-up events. BiH should also find new ways to encourage SMEs to get involved in the process of developing standards. It could introduce web-conferencing tools to decrease the cost of participation and develop case studies of SMEs that have benefitted from participating in standardisation.

Enterprise skills (Dimension 8a)

The overall score for this dimension stands at 2.70, on a par with its 2016 assessment and below the regional average (Table 14.17). Good efforts are noted in building skills intelligence across all entities which will allow for better targeting of funds to support SME training demand, particularly for sectors with growth potential.

Table 14.17. Scores for Dimension 8a: Enterprise skills

Dimension	Thematic block	BiH	WBT average
Dimension 8a: Enterprise skills	Planning and design	3.50	3.38
	Implementation	2.50	2.83
	Monitoring and evaluation	2.00	2.29
	Weighted average	2.70	2.87
BiH's overall score for Dimension 8a		2.70	2.87

State of play and key developments

The 2016 SBA assessment noted good developments in state-wide SME skills intelligence. Since then, these have been followed up in the FBiH as part of its SME development programme. In the RS, local development agencies have led on SME skills surveys in key sectors (industry, agriculture, food, hospitality and electronics), which is good practice, including the training offer by RARS for the metal sector. The Chamber of Commerce in the RS also continues to track SME manpower developments. A number of policy instruments identify poor technology and skills weaknesses in the agriculture sector, and concerns have been raised about the underinvestment in skills for the services sector.²⁴ It will be important for the authorities and training community, including universities, to respond to these challenges to avoid them becoming bottlenecks to implementing smart specialisation.

The wider preparations by the state to join the European Union will require dedicated support for small businesses to operate and compete within the EU internal market, where trade and business administration is increasingly digitalised. Good efforts, particularly by the Chamber of Commerce for Foreign Trade, have been made in providing training for SMEs to access international markets. However, training on digital skills among SMEs, including more developed online access to training, is weak.

The 2018-20 Economic Reform Programme highlights the low levels of innovation in the economy and raises concerns over brain drain, with BiH ranked 135th out of 137 economies for capacity to retain talent (WEF, 2017^[47]). Increasing skills levels through support for innovation will be important in the wider bid for competitiveness and growth, and particularly to retain talent. Universities therefore can no longer remain on the fringe of the wider drive for economic reform. With more concerted efforts in the Western Balkan region to kick-start smart specialisation, a more developed discussion at state and entity levels is required and should include: 1) the role of universities in local, regional and state level economic reforms; 2) interfacing medium- to higher-level vocational skills with innovation in targeted sectors; and 3) the potential for engagement and contribution of existing incubators.

Overall, across all the entities, policies and services to support the start-up ecosystem are under developed. Training services should more clearly distinguish between new start-ups, early-phase businesses and those with growth potential, which also require more

differentiated financial support. In particular, services need to meet the specific needs of women entrepreneurs.

The way forward for Dimension 8a

SME staff developments remain undeveloped within the wider economic reform agenda. If SMEs in Bosnia and Herzegovina are to compete effectively in the EU internal market, BiH needs to strategically build management and trade skills in those sectors with greater economic potential. This requires more sustained support for training at policy level, accompanied by monitoring and evaluation of training set against SME performance and wider economic development objectives.

The governments would be advised to take the following measures:

- **Embed skills development in economic strategies.** The next update of economic development strategies at entity level, including the 2019 Economic Reform Programme, should include management, vocational and regulatory training for SMEs in key economic sectors, and particularly focus on those sectors with growth and EU-trading potential. Incentives to encourage employers to develop talent within SMEs should be considered.
- **Hold policy dialogue on smart specialisation.** With more concerted efforts in the Western Balkans to kick-start smart specialisation, a more developed discussion is required at state and entity to include universities, vocational education and training skills in targeted sectors. The state's 12 incubators should be included in the policy dialogue.

Innovation policy for SMEs (Dimension 8b)

Bosnia and Herzegovina has the lowest score in the WBT region for this dimension, with a score of 1.86 (Table 14.18), which is well behind Kosovo (2.40) and Albania (2.48). What is perhaps most worrying is that it has made no visible improvements since the 2016 assessment (Figure 14.1).

Table 14.18. Scores for Dimension 8b: Innovation policy for SMEs

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 8b: Innovation for SMEs	Sub-dimension 8b.1: Policy framework for innovation	Strategic approach	2.25	3.46
		Co-ordination of innovation policy	1.44	2.97
		Implementation of innovation policy	1.86	3.04
		Weighted average	1.89	3.15
	Sub-dimension 8b.2: Government institutional support services for innovative SMEs	Incubators and accelerators	2.24	2.99
		Technology extension services for established SMEs	1.00	1.74
		Weighted average	1.74	2.49
	Sub-dimension 8b.3: Government financial support services for innovative SMEs	Direct financial support	2.53	3.76
		Indirect financial support	1.00	1.38
		Weighted average	1.92	2.81
	Sub-dimension 8b.4: SME and research institution collaboration and technology transfer	Innovation voucher schemes and co-operative grants	1.67	2.52
		Institutional infrastructure for industry-academia co-operation	1.67	2.72
		Intellectual property rights	2.50	3.00
		Weighted average	1.83	2.70
BiH's overall score for Dimension 8b			1.86	2.86

State of play and key developments

Policy framework for innovation

Research and development (R&D) and innovation policy is dealt with at the entity level. In the Republika Srpska, the key strategic framework for innovation is the recently adopted Strategy for Scientific and Technological Development (2017-20). Many of the measures it proposes are directly linked to the Innovation Centre in Banja Luka. In the Federation of Bosnia and Herzegovina, the only active document that discusses innovation is the SME Development Action Plan (2016-18). However, the Ministry of Development, Entrepreneurship and Crafts is leading efforts to develop the 2018-23 Innovation Strategy. Neither the RS nor the FBiH have any formal co-ordination mechanisms for innovation policy and no implementing agencies focusing solely on innovation. However, in the RS, RARS is co-ordinating the implementation of the Scientific and Technological Development Strategy.

Private sector actors are not systematically consulted when innovation policies are developed and there are no evaluation practices in place. The institutional set-up for innovation policy is highly decentralised across the various levels of government and there is no mechanism to co-ordinate these actors.

Government institutional support services for innovative SMEs

Both the RS and the FBiH have business incubators. The Innovation Centre in Banja Luka is the oldest initiative of this type in the RS, which now also has other four functional incubators, namely the Entrepreneurship Centre Banja Luka, Innovation Centre East Sarajevo and business incubators in Prijedor and Trebinje. There are 10 active incubators in the FBiH, which are directly supported by the government, despite a declining budget for this. In 2017, the FBiH's total investment in all forms of entrepreneurship support infrastructure was around EUR 500 000. There are reports of a number of incubators closing in the past two years, while some have stopped functioning as incubators because they allow companies to remain as tenants with no time limits.

In 2017, a new project was launched – Developing Accelerators to Provide Better Access to Innovation Finance for SMEs – supported by the Danube Transnational Programme (2014-20). Under this project, RARS is part of a 15-partner consortium of actors from 9 European countries and will receive about EUR 200 000 in total for its activities, with the goal of piloting an accelerator programme in the RS in 2018, based on good practices of partner consortium members.

There are no technology extension services in Bosnia and Herzegovina.

Government financial support services for innovative SMEs

Bosnia and Herzegovina's new Challenge to Change project, which started running in November 2016, has for the first time secured EUR 3.2 million for innovation enterprises. The project is open to SMEs from all over Bosnia and Herzegovina and Sweden, as well as start-ups that have innovative business ideas, products or services which may lead to increased employment, competitiveness and sustainable socio-economic development in BiH. With Swedish donor support, SERDA, together with RARS, have developed the conditions needed to launch the programme, which is planned to continue until 2020. Companies that meet the established criteria can receive a co-funding grant amounting to a maximum of 30 000 EUR, up to 50% of the investment costs (Challenge to Change, 2019^[48]). During the first call for proposals in 2017, 701 applications were submitted. The project shortlisted 80 of these and 28 were selected for funding, for a total investment of EUR 2.3 million.

SME and research institution collaboration and technology transfer

There have been no innovation vouchers or collaborative grants implemented in Bosnia and Herzegovina so far.

There are four science and technology parks in the FBiH – Zenica, Mostar, Tuzla and Sarajevo. The one in Zenica includes a specialised centre for new technologies and excellence in the wood industry – giving all companies in this sector access to the latest technological advances. The park in Zenica has 21 active resident companies, with over 70 employees. The INTERA tech park in Mostar is another great example of a private initiative which received public support – it has been operating successfully for ten years.

During this time, 38 companies have passed through the park and 360 jobs have been generated.

There is no legislation in Bosnia and Herzegovina to encourage technology transfer and commercialisation by defining the ownership of intellectual property and royalty split for publicly funded research.

The way forward for Dimension 8b

It is clear from this discussion that Bosnia and Herzegovina needs to significantly increase the importance of private sector innovation in its overall economic policy to improve policy formulation, co-ordination and implementation and to allocate budget to support such activities. The following measures will help:

- **Improve co-ordination of R&D and innovation policies.** Co-ordinating innovation policy is a challenge across all OECD countries, given the large number of stakeholders involved. In Bosnia and Herzegovina the different levels of government bring additional complexity. However, regardless of the level at which R&D and innovation policy is defined, it is crucial that it takes into account the complementary activities of other institutions, the needs of the private sector, and the capacity of the research sector to take part.
- **Secure direct funding for private sector R&D and innovation activities.** OECD countries typically use a mix of direct and indirect financing instruments for innovative SMEs but as Bosnia and Herzegovina has neither it should focus on creating a reliable, well-funded seed-funding instrument. This would support only the best proposals, providing enough funding for enterprises to conduct R&D activities, develop prototypes and test their ideas. Such an instrument could be modelled on the experiences of other economies in the WBT region, such as Serbia and North Macedonia, or OECD or EU member states. The Challenge to Change project is a good start, but runs the risk of remaining a one-off donor-based programme, like so many other initiatives in the country.
- **Implement an innovation voucher scheme.** Bosnia and Herzegovina lacks many of the elements needed to bring researchers and business together for R&D and innovation activities. Instead of tackling all of these challenges at once, BiH could consider starting with an innovation voucher programme, which provides small lines of credit to SMEs to purchase services from public knowledge providers with a view to introducing innovations in their business operations (OECD, 2010_[49]). This cost-efficient instrument has an extremely low administrative burden and is an excellent tool for bringing the two communities together. Ideally, it would be followed by a more significant funding instrument for joint research projects, but even without this element it is a pre-condition for creating dialogue between the two communities to examine avenues for co-operation and to create a basis for joint work.

SMEs in a green economy (Dimension 9)

Bosnia and Herzegovina is one of the few WBT economies to increase its score in this dimension (Figure 14.1) – up slightly from 2.29 in 2016 to 2.40 in 2018 (Table 14.19). Although SME greening seems to be gaining momentum in BiH, its overall performance is still low.

Table 14.19. Scores for Dimension 9: SMEs in a green economy

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 9: SMEs in a green economy	Sub-dimension 9.1: Framework for environmental policies targeting SMEs	Planning and design	3.47	3.81
		Implementation	2.50	2.56
		Monitoring and evaluation	2.00	2.12
		Weighted average	2.69	2.85
	Sub-dimension 9.2: Incentives and instruments for SME greening	Planning and design	1.67	2.32
		Implementation	2.42	2.76
		Monitoring and evaluation	2.25	1.72
		Weighted average	2.16	2.42
BiH's overall score for Dimension 9			2.40	2.61

State of play and key developments

Framework for environmental policies targeting SMEs

In Bosnia and Herzegovina, SME greening policies are devised and implemented at the entity level, with no state-level institutions in charge of promoting the green economy. Strategies and action plans that include goals for the green economy are also adopted at the entity level. The newly adopted Strategy for Rural Development (2018-21) is the only state-level strategy that includes some environmental protection measures that could be relevant for SMEs. These actions are aimed at promoting and certifying organic production, as well as reducing the carbon footprint of agricultural production (e.g. the use of renewable energy sources in agriculture). Concrete activities, a clear timeline and the institutions responsible for their implementation have yet to be determined – however, the strategy specifies that the measures will be implemented at the entity level.

At entity level, only the RS has environmental policies that encompass SMEs. Since the last assessment, the RS has introduced SME greening into its 2016-20 SME Strategy. One of the goals of the strategy is improved environmental performance among SMEs. Government actions focus on information campaigns and training to raise SMEs' awareness of environmental issues and help them obtain all the information they need to “go green”. The government also envisages introducing eco-labelling to increase market recognition of good environmental practices. The strategy promotes better energy efficiency among SMEs and provides financial support in this area. Implementation of the planned activities has been rather slow, mainly due to significant delays in mobilising funds and reliance on donor support for SME greening.

In the FBiH, as the previous assessment also found, environmental policies are separated from SME policies so there are no clearly defined environmental policies targeting SMEs. The FBiH's comprehensive Environmental Protection Strategy, which runs until 2030, does not contain SME-specific actions or targets, but it does indirectly promote eco-

efficiency and eco-innovation among businesses, and by extension among SMEs. FBiH's Waste Management Strategy (2008-18) also includes environmental policy elements that are relevant to SMEs, such as promotional activities on waste prevention and recycling, and guidance regarding cleaner production actions.

Incentives and instruments for SME greening

Both entities have operational environmental protection funds which have increased the scope and outreach of their programmes and activities since the last assessment. They both offer environmental information and support to help interested parties and beneficiaries improve their environmental performance. However, they still mostly focus on large – mainly infrastructural – projects.

In the RS, the SME Strategy foresees the introduction of financial incentives for SME greening which will be realised through projects by the Fund for Environmental Protection and Energy Efficiency. To date however no activities have been implemented to achieve this.

Since the last assessment, BiH has begun recognising improved environmental performance among SMEs. The FBiH has re-established its awards for SME achievements in the area of environmental protection. Since 2008, as part of Jahorina Fest (the International Festival of Documentary Movies, Tourism and Ecology) the environmental protection funds of the FBiH and the RS give up to 10 awards for the best ecological projects of the year in BiH in different categories, including for SMEs. In addition, in 2017, the Green Centre for Development and Support, an NGO from Tuzla, and the US Embassy in BiH, introduced the BIH Green Awards, which are awarded in four categories: 1) businesses; 2) cities/municipalities; 3) NGOs and foundations; and 4) citizens. The awards go to entities that successfully promote real environmental values and may motivate and encourage the others to do the same (CRP, 2017^[50]).

The way forward for Dimension 9

Bosnia and Herzegovina has undertaken some steps to promote and support SME greening. Going forward, the government should consider the following:

- **Implement measures to help SMEs improve their resource efficiency.** Environmental policies specifically designed for SMEs have become part of the SME Strategy in the RS for the first time, but implementation seems to be rather limited. The RS is therefore invited to improve its realisation of the planned measures and ensure regular monitoring. As none of the strategic documents in the FBiH includes SME greening measures, the FBiH should ensure its environmental policies are not detached from SME development. The FBiH government is recommended to introduce SME greening measures in its Environmental Protection Strategy.
- **Increase financial support for SME greening.** Although financial incentives are part of the new SME Strategy in the RS, it is not clear what type of incentives will be used or how they will be financed. It will be essential for the RS to decide what type of financial support to offer SMEs, mobilise the funds accordingly and carefully plan these schemes. Although the FBiH has no such incentives, both entities have very active environmental protection funds though they do not have a particular focus on SMEs. This should be addressed by expanding their scope to also include SMEs through specific financial programmes that would support

SME greening. The government might also consider facilitating SMEs' access to green finance by introducing a dedicated loan guarantee scheme or subsidising interest rates for green project loans.

Internationalisation of SMEs (Dimension 10)

Bosnia and Herzegovina has made marginal improvements in its support for the internationalisation of SMEs. Since the 2016 assessment, its score has increased from 2.31 to 2.57 (Figure 14.1), but remains well below the regional average (Table 14.20). Increased support to export promotion (Sub-dimension 10.1) and global value chains (Sub-dimension 10.2) have contributed the most to BiH's enhanced performance, but a lack of co-ordination among institutions has hindered further progress.

Table 14.20. Scores for Dimension 10: Internationalisation of SMEs

Dimension	Sub-dimension	Thematic block	BiH	WBT average
Dimension 10: Internationalisation of SMEs	Sub-dimension 10.1: Export promotion	Planning and design	4.33	4.86
		Implementation	3.70	4.24
		Monitoring and evaluation	2.19	3.01
		Weighted average	3.59	4.18
	Sub-dimension 10.2: Integration of SMEs into global value chains	Planning and design	2.07	3.58
		Implementation	1.86	3.08
		Monitoring and evaluation	1.00	1.76
		Weighted average	1.75	2.97
	Sub-dimension 10.3: Promoting the use of e-commerce	Planning and design	2.71	3.45
		Implementation	1.33	2.26
		Monitoring and evaluation	1.00	1.36
		Weighted average	1.68	2.44
BiH's overall score for Dimension 10			2.57	3.43

State of play and key developments

Overall, the internationalisation of SMEs in Bosnia and Herzegovina has increased over the course of this assessment period. For example, SMEs' share of exports increased from 59% to 61% of total exports between 2013 and 2017. In the same period, the value added by SMEs increased by 1.3 percentage points, while the value of exported goods and services, reached 36% of GDP in 2017 compared to 34% of GDP in 2013 (World Bank, 2018^[1]).

The cost of border compliance when importing and exporting remained unchanged between 2014 and 2017. Border compliance costs for exports stood at USD 106, between the OECD average of USD 164 and the EU average of USD 85. The costs for importing, at USD 109, were also between the averages of the OECD (USD 137) and the EU (USD 29) (World Bank, 2018^[1]).

Export promotion

Bosnia and Herzegovina has improved its support for export promotion, although it still performs below the regional average. One noticeable development over the course of this assessment period has been the 2016 agreement with the European Union on the economy's participation in COSME (2014-20).

Export promotion programmes in the Federation of Bosnia and Herzegovina are linked to the 2016-18 Action Plan for the Realisation of the Project Development of SMEs. In the Republika Srpska, measures for export promotion are planned in the SME Strategy and

the Foreign Investment Encouragement Strategy 2016-20. There is no state-level strategic framework for export promotion, although activities are being undertaken.

At the state level, the Export Promotion Chamber of the Foreign Trade Chamber supports the development of export promotion policies with the Ministry of Trade and Economic Relations. It also co-operates with other agencies, such as the Foreign Investment Promotion Agency, regional chambers of commerce, and entity-level ministries. Although it has autonomy over its budget and human resources, it is limited in both staff and funds. The Foreign Trade Chamber provides a narrow range of activities for SMEs, such as support for their participation in international trade fairs, and foreign market research. Its website provides sparse information, and makes no reference to support mechanisms available for SMEs. In terms of financial support, in 2017 the Foreign Trade Chamber allocated grants totalling about EUR 385 000 for the organisation of trade fairs in Bosnia and Herzegovina and about EUR 187 000 for participation in international trade fairs. The Foreign Trade Chamber also acts as European Enterprise Network (EEN) co-ordinator in the Federation Bosnia and Herzegovina.

In the FBiH, the FMRPO provides trade policy information, commercial intelligence, and co-financing support, e.g. for product development support and training to SMEs. Moreover, under its Strengthening the Competitiveness of SMEs scheme, it also provides export promotion support to SMEs. In total, it has allocated about BAM 2 million (EUR 1.02 million) to this scheme for 2017, of which about BAM 300 000 (EUR 153 000) were allocated to export promotion support.

In the RS, RARS acts as the EEN co-ordinator, mostly providing technical support and organising SME promotion events.²⁵ The RS also has a network of representation offices in Austria, Belgium, Germany, Greece, Israel, Russia, Serbia and the United States, which organise periodic training for domestic SMEs on export opportunities to the relevant country. Meanwhile, the Chamber of Commerce and Industry of RS also supports the annual participation of business entities in domestic and international trade fairs in co-operation with chambers of commerce in the region and abroad, diplomatic and consular missions, the representation offices of the Republika Srpska and international organisations. Previously, the Chamber of Commerce and Industry of RS also supported export promotion activities, while the Ministry of Industry, Energy and Mining provided financial support to improve SME competitiveness and export readiness. However, there have been no recent financial support programmes in the RS. One noticeable development during this assessment period was the establishment of the export information centre web portal (www.izvozinfor.net) in the RS, providing information on export opportunities, legal regulations and support for exporters.

Financial support to SMEs for export promotion activities remains patchy across Bosnia and Herzegovina.

In Bosnia and Herzegovina, trade finance guarantees to SMEs are available through banks, and many banks also offer letters of credit (EIB, 2016^[51]). In the RS, trade finance guarantees are available through the Guarantee Fund of Republika Srpska, which offers a repayment period of up to two years for working capital and up to one year for loans for pre-export financing. The guarantee is up to BAM 300 000 (around 153 000) for working capital and has a grace period of up to 12 months for working capital to prepare exports (Guarantee Fund of the Republic of Srpska, 2015^[52]).

Integration of SMEs into global value chains

There are programmes to support SME integration into global value chains at the entity level in BiH, especially in the Republika Srpska. The 2016-18 action plan as part of the strategy document Development of Small and Medium Enterprises in the Federation of Bosnia and Herzegovina 2009-2018 includes measures to support projects for developing clusters and value chains, while in the RS measures for cluster support to promote the internationalisation of SMEs are covered in the 2016-20 SME Strategy.

However, efforts to carry these initiatives forward remain fragmented and sporadic, and rely mostly on international donor financing. In the FBiH, despite having proposed programmes, the government did not mobilise a budget for it over the assessed period, citing the low number and quality of applications.

Some programmes to address SME positioning in value chains have been carried out in the past through international donors such as USAID.²⁶ Various initiatives have fostered cluster development in the RS, all implemented by RARS. RARS current activities to support cluster development primarily involve organising events. Under the auspices of the European Entrepreneurship Network, and in co-operation with Development Agency of Serbia, RARS held two international business meetings for companies and clusters in 2016 and 2017. In the framework of the Public-Private Dialogue and Partnership project in 2016, it also organised meetings with members of the wood processing industry and forestry cluster to improve co-operation, joint promotion and commercialisation. During 2016, RARS provided professional and technical support for strategic planning and project management to the Banja Luka information technology (IT) cluster. In the same year, it also supported the preparation of project proposals, promotion of IT clusters and other areas. RARS has also provided support for the development of clusters in the tourism sector by participating in the meeting of representatives of tourist organisations from several cities across the RS. In August 2016 a meeting was held within the 11th Economy and Tourism Fair in Derвента to share information and examine the possibilities for establishing tourism clusters.²⁷

The perceptions of cluster development in Bosnia and Herzegovina improved strongly between 2014 and 2018, as noted in the World Economic Forum's *Global Competitiveness Index* (WEF, 2017^[53]).

Promoting the use of e-commerce

E-commerce is currently not well advanced in Bosnia and Herzegovina, though it has significant potential for development. In 2018, the economy had a relatively high percentage of SMEs selling online, at 21% compared to the EU average of 17%²⁸ (EC, 2018^[54]). However, of the six WBT economies for which data was available, Bosnia and Herzegovina had the second lowest figure for Internet purchases by individuals in 2018 (18% of respondents), more than three times lower than the EU average of 60% (EC, 2018^[54]). However, the United Nations Conference on Trade and Development's (UNCTAD) B2C E-commerce Index ranked BiH in the top 10 for transition economies in 2018 (UNCTAD, 2018^[55]).

Currently, BiH has no institution responsible for promoting e-commerce. The Information Society Strategy 2017-2021, developed by the Ministry of Communications and Transport and adopted in May 2017, encompasses a broad number of areas that could strengthen the operational environment for e-commerce, including digital literacy, Internet access, and increased online services. However, no financial support tools have

been developed to accelerate the adoption of information and communications technology (ICT) and digital practices by SMEs (OECD, 2018^[7]).

The legal framework for e-commerce remains patchy: an e-payment law has been drafted at the national level, while the RS has adopted e-business legislation that covers e-payments. The RS has a legal framework for consumer protection in e-commerce and has implemented a consumer protection programme. At the state level, the legal framework for consumer protection in e-commerce is out of date, while no framework exists in the FBiH (OECD, 2018^[7]).

RS's Agency for the Information Society provides information on legislation and standards relevant for SMEs' engagement in e-commerce on its website; the FBiH has no equivalent resource.

The way forward for Dimension 10

In order to further promote SMEs' access to and competitiveness in international markets, Bosnia and Herzegovina should consider the following policy recommendations:

- **Increase SMEs' uptake of programmes aimed at supporting cluster and local supplier quality.** While both entities and the Foreign Trade Chamber have provided some export promotion support to SMEs, both entities could consider strengthening their efforts to support SMEs' integration into GVCs and clusters by going beyond current support programmes. In particular they should intensify their efforts to proactively facilitate information flows along the entire supply chains for involving SMEs. They should take on the role of knowledge broker concerning the needs of upstream and downstream enterprises, and encourage multinational enterprises to share their road-maps for future product and process development with their SME partners. Moreover, the relevant institutions should provide access to accurate information on market opportunities for subcontracting and potential foreign partners through market reports and databases, trade fairs, exhibitions abroad, and electronic trading platforms or subcontracting exchanges.
- **Strengthen the provision of information on export promotion, cluster and other internationalisation support programmes.** While the RS export information centre is a step in the right direction, Bosnia and Herzegovina could provide information on all state, entity and canton-level programmes in one single web portal. In addition such a portal should provide information on the current legal framework and include step-by-step information about exporting, with access to the forms needed, as well as links to other relevant sources, such as cluster platforms and relevant government agencies.
- **Complete the legislative and strategic framework for e-commerce and develop formal mechanisms to encourage SMEs to adopt e-commerce.** The legislative and strategic framework for e-commerce should aim to harmonise entity and cantonal legislation. Policy makers should ensure that BiH's administrative capacities are sufficient and that investment in ICT infrastructure will enable SMEs to benefit from the possibilities of e-commerce. To this end, policy makers could also implement programmes to facilitate SME uptake of e-commerce opportunities, for example by supporting access to e-commerce websites and portals via co-financing schemes.

Conclusions

Bosnia and Herzegovina's progress in the implementation of the Small Business Act during the assessment period has been good. Nevertheless, in all 12 policy dimensions, it still scores below the regional average.

This picture is primarily a result of the lack of a co-ordinated approach to SME policy planning and implementation across different levels of administration. Better co-ordination could create synergies among different actors, and make better use of resources. There is still no single economic space in place across BiH that is conducive to entrepreneurship and investments.

With a whole-of-government approach, the current initiatives supporting SMEs would be much more impactful, and achieve the desired outcomes.

Notes

¹ The WBT region refers to the six pre-accession Western Balkan economies (Albania, Bosnia and Herzegovina, North Macedonia, Kosovo, Montenegro, and Serbia) and Turkey. Unless otherwise specified, reference to the "region" in this publication implies these seven economies.

² The sector includes defence, education, social services and other public administration.

³ For more information about the OECD FDI Regulatory Restrictiveness Index, see OECD (2018^[7]).

⁴ In EU countries, SME envoys are appointed by the national government to report on the uptake of the SBA and to promote SMEs' interests through government bodies. Such SME envoys do not exist in pre-accession countries.

⁵ Smart specialisation originated in the EU as a concept for stimulating innovation-driven regional growth. Smart specialisation strategies are about enabling regions to turn their assets, strengths and competitive advantages into marketable goods and services, and ultimately economic growth. Human capital, knowledge dissemination and transfer, as well as support to entrepreneurship, are all key elements in successful implementation of smart specialisation strategies. For more information, please see Chapter 9 on enterprise skills and Box 13.1 in Chapter 10 on innovation policy for SMEs.

⁶ Published in the Official Gazette of FBiH No. 29/03, 32/04 and 28/06.

⁷ Official Gazette of FBiH 29/03.

⁸ The constitutional court has addressed the issue back to parliament to find "proper" resolution because of the contradiction between these two articles. Article 33's case is about preferential payment of eight salaries of workers before all other unsecured creditors. Article 40's case is about the absolute priority of payment to bankruptcy case proceedings' costs before payment of any other creditor.

⁹ <https://www.paragraf.ba/propisi/fbih/zakon-o-stecajnom-postupku.html>.

¹⁰ Official Gazette of the RS 16/16.

¹¹ Official Gazette of BDBiH 1/02.

¹² For more information: <http://www.preduzetnickiportalsrpske.net/danubechance2-0/> and <http://www.interreg-danube.eu/approved-projects/danubechance2-0>.

¹³ <https://ekonsultacije.gov.ba/>.

¹⁴ Official Gazette RS No, 106/15.

¹⁵ Idem.

¹⁶ FBiH Government: The Law on Companies in the Federation of BiH, “Official Gazette of FBiH: https://advokat-prnjavorac.com/zakoni/Zakon_o_privrednim_drustvima_FBiH.pdf.

¹⁷ Law on value added tax in BiH - Official gazette BiH No. 100/2008.

¹⁸ <https://advokat-prnjavorac.com/zakoni/Zakon-o-porezu-na-dohodak-Republike-Srpske.pdf>.

¹⁹ Unincorporated businesses refer to small entrepreneurs as defined in Article 21 of the Law on Income Tax (Official Gazette of the Republic of Srpska, No. 60/15). Businesses need to meet three conditions: 1) no more than 3 employees (including the owner); 2) no partnerships; and 3) annual income of less than BAM 50 000 (EUR 250 000).

²⁰ <http://www.uplusu.ba/>.

²¹ The European Union adopts legislation (EU Directives) that defines essential requirements in relation to safety and other aspects of public interest which should be satisfied by products and services being sold in the Single Market.

²² State institutions have the competence to implement a quality infrastructure system in Brčko District.

²³ These include 66 testing laboratories, 2 medical laboratories, 8 calibration laboratories, 2 product certification bodies and 38 inspection bodies.

²⁴ BiH Economic Reform Programme 2017-2019).
<http://www.dep.gov.ba/naslovna/Archive.aspx?pageIndex=1&langTag=en-US>

²⁵ In addition to the agency as co-ordinator, members of the European Entrepreneurship Network of the Republic of Srpska include the Chamber of Commerce of the Republic of Srpska, the University of Banja Luka, the University of East Sarajevo and the Innovation Center Banja Luka.

²⁶ Fostering Interventions for Rapid Market Advancements was a USD 21 million activity financed jointly by USAID and the Swedish International Development Cooperation Agency to support SMEs in the targeted sectors of wood processing, tourism and light manufacturing/metal processing in BiH. The objective was to increase sustainable economic growth as measured by increased sales, exports, sustainable employment and access to finance. The project ran from September 2009 to May 2015 and the activity was implemented by a consortium led by Cardno Emerging Markets USA, Ltd.

²⁷ Representatives from Doboj, Brod, Teslic, Modriče, Šamac, Kozarska Dubica and Laktaši attended. The meeting primarily served to provide legal information on establishing clusters.

²⁸ The Eurostat indicator refers to SMEs, excluding in the financial sector, employing between 10 and 249 employees.

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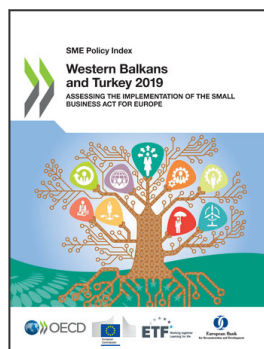
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From:

SME Policy Index: Western Balkans and Turkey 2019

Assessing the Implementation of the Small Business Act for Europe

Access the complete publication at:

<https://doi.org/10.1787/g2g9fa9a-en>

Please cite this chapter as:

OECD, *et al.* (2019), “Bosnia and Herzegovina: Small Business Act profile”, in *SME Policy Index: Western Balkans and Turkey 2019: Assessing the Implementation of the Small Business Act for Europe*, OECD Publishing, Paris.

DOI: <https://doi.org/10.1787/a09405ef-en>

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