

THE ROLE OF THE GOVERNMENT IN ENTREPRENEURSHIP DEVELOPMENT: EVIDENCE FROM BOSNIA AND HERZEGOVINA

Zijad Dzafic *, Amra Babajic **

ABSTRACT

In recent decades, economic growth in countries around the world has become increasingly dependent on the dynamism of small and medium sized enterprises (SMEs). This is especially important in the transition economies. The creation of a new SME sector in Bosnia and Herzegovina (BiH) as a transition country may play an important role in the process of economic regeneration and job creation. The paper sets out an approach to analyzing the development of SMEs in BiH. We have focused on (i) attitudes of entrepreneurs in the private sector towards the role of government in SME development through provision of assistance to SMEs in BiH, (ii) the business environment in which firms operate, and (iii) attitudes of the employed in government sector towards the role of government in SME development through the provision of assistance to SMEs in BiH. The paper reviews the literature on these three approaches and available evidence on relevance to understanding the performance of SMEs as main agents of entrepreneurship in the BiH.

Keywords: *Institutions, entrepreneurship, SME, transition, growth*

JEL: P2, O40, H00

1. INTRODUCTION

The success of an enterprise also depends on the support provided by its state. By its regulations it can create an attractive and

easier climate for business enterprises on the one hand, while on the other hand the state can be a major limiting factor for the establishment and development of enterprises. In the entrepreneurial economy the state is not an entrepreneur, it is rather supposed to protect, with all its legal force, every business venture. The state, its institutions and officials do not act as executive authorities, but are seen as a necessary administrative service for successful business. Their responsibilities are to provide a stimulating business environment and development support to SMEs, by stimulating legislation, improving institutional capacities, rendering adequate measures of economic policy, and establishing the necessary infrastructure.

Developed countries have long-standing experience and good strategies to support entrepreneurship, while the underdeveloped and developing countries make beginner's steps in the development of strategies which are of great importance for the development of this sector. In order to achieve faster regional and local economic development, the world, the countries in Southeast Europe and BiH (to a lesser degree) recognized the need for building entrepreneurial infrastructure and expanding the network of its support institutions. Therefore, the development of enterprises depends largely on institutional, physical and financial infrastructure that a country has. The higher level of infrastructure development, the easier factor it represents in

* Faculty of Economics, University of Tuzla, Bosnia and Herzegovina, zijad.dzafic@untz.ba

** Faculty of Economics, University of Tuzla, Bosnia and Herzegovina, amra.babajic@untz.ba

the development of entrepreneurship in the country and vice versa.

According to Doing Business (World Bank, 2016) ranking for 2016, for most factors observed BiH's position was worse than for 2015, its overall ranking is by 5 positions lower, and in the observed four-year period the country recorded the lowest ranking in terms of: starting a business (175), obtaining construction permits (171), paying taxes (154), protecting investors (66) etc.

When it comes to *starting a business* criterion, the comparison with the average data for the countries in Europe, Central Asia and the Organisation for Economic Co-operation and Development (OECD), shows that our country lags behind by the number of procedures required for starting a business (a total of 12 procedures, while the average number for the countries of Europe and Central Asia is 5 and the OECD 4.8). One of the segments that certainly discourage entrepreneurs in BiH is the time needed for starting a business, which is 67 days, while the average in Europe and Central Asia is 12.1 and in OECD countries 9.2. Start-up costs are 2.5 times higher than in the compared countries, while the minimum paid-in capital is up to 4 times higher than the average for the observed regions. The total cost of business registration (various fees, certificates and forms) in BiH amounts to about BAM 1,190.

According to the Global Competitiveness Report 2015-2016 (World Economic Forum, 2016), BiH is ranked 111th out of 140 ranked countries, with 3.7 points out of 7. The most problematic factors of the business environment in BiH as rated by the World Economic Forum are: undeveloped institutions (127), labor market efficiency (131), undeveloped infrastructure (103), access to finance, government instability, tax

rates and inefficient tax system, inefficient bureaucracy, corruption, and so on.

The presented data show that the business environment in BiH is unfavorable, as evidenced by the comparison with other countries as well as with regional and global averages. Therefore it was necessary to examine why there has not been progress in this field, for many years, and if private and public sectors perceive this as a problem, because only after clear identification of the problem is it possible to start solving it. So, the main goal of this paper is to determine the perceptions of private and public sectors about the role of the state and entrepreneurship development in terms of administrative and regulatory obstacles.

The first part of the paper provides a theoretical background and literature review on the importance of the role of the state in entrepreneurship development, focusing on the obstacles (regulatory and administrative) in business. The second part of the paper represents the implemented research methodology. After that, the paper brings there search results and discussion of perceptions of the SME owners on the one hand and government and administration representatives in BiH on the other hand in creating positive environment for entrepreneurship.

2. Theoretical framework of research - literature review

The new ideology of neoliberalism emphasizes the role of SMEs as promoters of a "healthy" business climate, economic efficiency and power for economic growth, especially in small, developed countries, and even more so for countries in transition. For almost three centuries, economists have been making contributions to the academic

literature on entrepreneurship (Cantillon, Mill, Say, Knight, Schumpeter, Krizner, Casson, Shackle etc.) and advanced our understanding of the entrepreneur's role in the economy.

Entrepreneurial activity behind SMEs has been increasingly recognized as a major driving force for innovation and economic growth in all economies (Audretsch 2001). SMEs have a particularly important role to play in the process of job creation in transition economies since they may generate jobs for those who are dismissed from large firms undergoing restructuring or privatization (Tyson et al., 1994; Bartlett and Hogget 1996; Kolodko, 2000; Dzafic 2007, 2014, Wichkam 2006). Thurik and Wennekers (2004) characterize this as a shift from a 'managed economy' of large firms in the immediate post WWII years, to an 'entrepreneurial economy' of small and medium sized firms in the 1980s onwards. They also played an important role in the Southern European countries such as Italy, where SMEs organized in industrial districts were the main agents of the remarkable economic growth of the Emilia Romagna region in the 1980s and 1990s. The emphasis on the central role of SMEs has more recently come to dominate policy thinking throughout the European Union (EU) (Bartlett et al. 2013).

Van Praag and Versloot (2007) have identified four economic benefits of entrepreneurship: job generation, innovation, productivity and growth. SMEs are now recognized by researchers, analysts and policymakers as central to economies across the world, through their contributions to wealth creation, income generation, output and employment (OECD 2011).

As a result, the success of SMEs and entrepreneurship has become increasingly

important to governments and public administrators (Robert and Michael, 2012). The relationship between entrepreneurship and economic growth has seen increased interest at the local, state, and national levels, and recent studies have shown that the contribution of the entrepreneurial sector to employment and GDP is increasing (Minniti 2008; Kumar & Liu, 2005) and has important social implications (Chell 2007).

Also, there are numerous studies and scientific papers that confirm the positive correlation between entrepreneurship and economic growth (see Naude 2008, Wennekers, van Stel, Carree and Thurik 2007, etc.). However, some authors such as Baumol (1990) believe the opposite. He claims that there are different forms of entrepreneurship that could adversely affect economic growth in some countries, such as entrepreneurial forms of unproductive and destructive character. Many authors have documented the existence of a positive relationship between the rate of entrepreneurship and economic growth and development (see Thurik and Wennekers 2004).

Over the last three years, the Western Balkan countries have registered moderate progress in several areas, including the institutional framework for SME policy, regulatory reform and administrative simplification, company registration, entrepreneurial learning and business start-up processes, etc. They have made significant progress in skills development and export promotion. On the other hand, on average, their performance on the provision of SME support services slightly deteriorated (SME Policy Index 2012).

In comparison to the development of SMEs of the developed countries, development of SMEs and entrepreneurship in Western Balkan countries are in some kind of a

schizophrenic position in the economy, especially in Bosnia and Herzegovina. No doubt, they inevitably need government assistance. SMEs cannot develop without government assistance at all levels and SMEs cannot give up to the invisible hand of the market. However, bribery, nepotism, conflict of interest, and swapping of favors are common in education, health care, and other areas of public administration. State and entity legislatures are considering several anticorruption bills and amendments, but a lack of political will has slowed adoption. Indicative of this laxity, the country reached the end of its 2009–2014 Strategy for the Fight against Corruption with only 9.8 percent of the planned measures fully implemented (Transparency International 2014)

In the end, BiH currently lags behind its peers in the Western Balkan region in its SME policies. There is still no state-level strategy for innovation. The lack of co-operation between state and entity level institutions remains a major obstacle to the development of a solid policy framework for SME internationalization. The unemployment rate stayed at 27.5% in 2014, the second highest rate in the region after Kosovo. The unemployment rate of youth is 60% and the rate of grey economy is about 30-50% of GDP (SME Policy Index: Western Balkans and Turkey, 2016).

3. Research concept

3.1. Methodological approach and defining hypothesis

The subject of this research is limited to the tools of economic politics in the development of entrepreneurship through removing administrative and regulatory obstacles, and therefore, the research hypothesis is postulated as follows:

H₁: There is a significant difference in perception of private and public sectors about the role of the state in entrepreneurship development in terms of administrative and regulatory obstacles.

For the purposes of the research, a structured questionnaire was sent to 250 SMEs and to the relevant government institutions at the state, entity and cantonal level such as Federal Ministry of Development, Entrepreneurship and Crafts; Federal Ministry for Programming Development; Agency for Development of Small and Medium Sized Enterprises of Republic of Srpska; Government of Brcko District – Development Grant Fund of Brcko District; Federal Ministry of Energy, Mining and Industry; Ministry of Foreign Trade and Economic Relations of BiH, as well as to ten cantonal ministries of entrepreneurship. The descriptive and multi-variation statistical analysis has been conducted on the collected primary data. The subject research is a part of the bigger scientific research paper realized at the Faculty of Economics at the University of Tuzla, during 2014.

3.2. Research subject and goals

In order to understand and explain the aforementioned problem, it is essential to objectively and empirically explore its origins and identify the appropriate instruments for solving it. Therefore, the subject of this research is establishing the position of the SME sector in BiH and pinpointing the main obstacles in the development of the SME sector. In order to prove the hypotheses, it is necessary to realize the following research goals:

Goal 1: Determine the attitudes of the private sector towards the role of the state in entrepreneurship development

Goal 2: Determine the attitudes of the public sector towards the role of the state in entrepreneurship development

Goal 3: Based on the results of the empirical research, provide recommendations for the future steps of state intervention in strengthening entrepreneurship.

4. Empirical findings

The primary data on the role of economic policy tools in the development of entrepreneurship in BiH have been collected through the method of a written structured questionnaire. The questionnaire, as a research instrument, has been divided into two parts: the first part filled by enterprise management and the second part filled by the representatives of government institutions. The collection of data has been conducted on the foundation of a proportional stratified sample. The whole population has been

Considering that the population is extremely large (39,579 enterprises), if we used the fraction of selection of 5%, then the size of the sample would amount to 1,979, and such sampling under actual conditions would be hardly feasible. For the subject research, we have decided the sample to include 250 units. The structure of the planned proportional stratified sample according to the number of employees, that is, according to the size of enterprise, has been presented in Table 4.1.

After that, the selection of sample units has been conducted. Each enterprise has been given an unrepeatable number through the record in the database. These numbers from the enterprise database for the three selected strata (micro, small and medium enterprises) have been recorded into the software for generating random sample. Through the random sampling of the stratum units, we have formed a list of 197 enterprises from the

Table 4.1. Size and structure of the sample of the surveyed SMEs

Group	Enterprise size	Stratum		Sample		
		Number of SMEs	%	%	Number of SMEs	Number of SMEs in the sample
1	Small enterprises (<50 employees)	37,641	95.1	95.1	237.75	238
2	Medium enterprises (≥50 employees)	1,938	4.90	4.9	12.25	12
Σ		39,579	100	100	250	250

Source: Data on the number of SMEs has been taken from the register for 2010, of the Bureau of Indirect Taxation of BiH

divided into for strata: micro, small, medium and large enterprises, and then, by data filtration, the large enterprises have been excluded from the sample, considering the research subject. Micro, small and medium enterprises then underwent the random sampling where a certain number of units has been selected that was proportional to the stratum size.

micro enterprise stratum, a list of 41 enterprises from the small enterprise stratum, and a list of 12 enterprises from the medium enterprises stratum. In the same way, for every stratum, a reserve list has been formed, where the immediate next enterprise was selected in case that an answer was not received from the enterprises from the primary list.

The surveying of the private enterprise management was conducted in the time frame of 6 months (May-November 2014), and the response rate (filled questionnaires) was 54%. In the frame of surveying government institution, the research has been conducted in the ministries responsible for entrepreneurship development at the level of BiH: Federal Ministry of Development, Entrepreneurship and Crafts; Federal Ministry for Programming Development; Agency for Development of Small and Medium Sized Enterprises of Republic of Srpska; Government of Brcko District – Development Grant Fund of Brcko District; Federal Ministry of Energy, Mining and Industry; Ministry of Foreign Trade and Economic Relations of BiH, as well as to ten cantonal ministries of entrepreneurship. The rate of response (filled questionnaires) by government institutions was 62.5%.

For the purpose of this research, a descriptive statistics (arithmetic medians, frequencies) was used, and for determination of quantitative variations at the multi-variation level and determination of statistically significant variations in the attitudes of the surveyed from the private and the

government sectors, the discriminant analysis was used.

4.1. Discussion

4.1.1. The role of the state in entrepreneurship development in terms of regulatory and administrative obstacles (SME perceptions)

By removing barriers to the registration and operation of companies, the state certainly can influence the creation of a favorable business environment for the development of entrepreneurship which in this paper refers to the regulatory and administrative, and financial barriers. Generally speaking, the state can facilitate business operations by the following: eliminating/reducing bureaucratic and administrative barriers such as simplifying regulations; speeding up land registration procedures (in terms of reducing the time limits for the issuance of various approvals, zoning permits, construction permits, etc.); and reducing bureaucratic obstructions (slowness, rigid functioning of various bodies such as inspection services, institutions dealing with the issuance of various license, certificates, etc.).

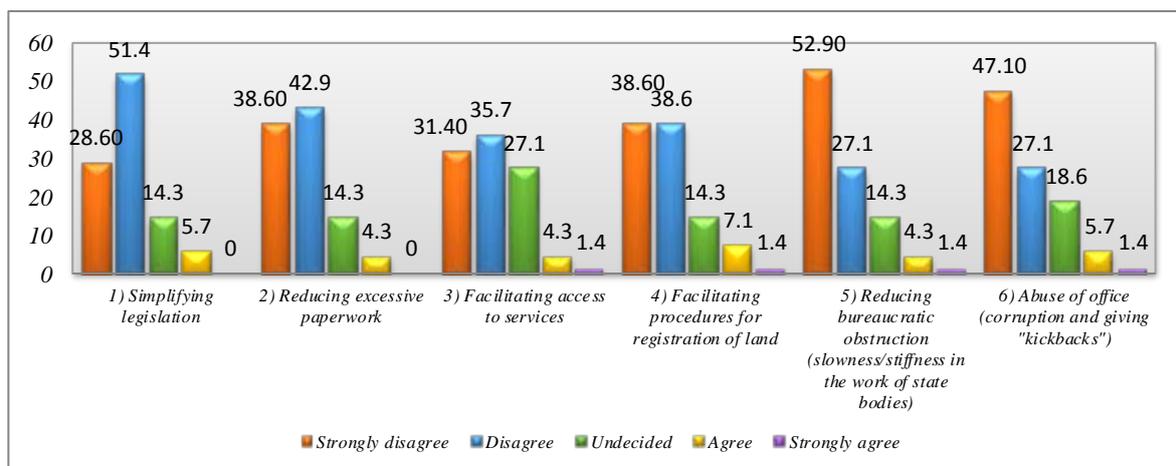


Figure 4.1. Perceptions of private sector about the role of the state in entrepreneurship development

Authors' research

The majority of respondents from the private sector are dissatisfied with the state's role in the elimination of administrative and regulatory barriers. As many as 42.9% of the respondents answered "do not agree", and 38.6% of them answered "strongly disagree" with the claim "State is working on reducing excessive paperwork necessary for the registration and operation of an enterprise". A high 51.4% of the respondents opted for "do not agree" and 28.6% of them answered "strongly disagree" referring to the claim "State is working on simplifying legislation related to the registration and operation of enterprises". A high level of disagreement was registered with the claims: "State is reducing bureaucratic obstruction (slowness/ stiffness in the work of state bodies)", with 52.9% of the answer "strongly disagree" and 27.1% of the answer "do not agree"; and "state works to reduce abuse of office (corruption and giving "kickbacks")" with 47.1% of the answers given being "strongly disagree" and 27.1% of the answers offered "do not agree". It can be

concluded that, when it comes to reducing the administrative and regulatory barriers, there is a high level of disagreement with the claims, which means that the participants from the private sector are not satisfied with legislation and procedures, the volume of paperwork, reducing bureaucratic obstruction, etc. The ratio of expressed strong agreement to a high degree of expressed disagreement can be considered negligible.

4.1.2. The role of the state in entrepreneurship development in terms of regulatory and administrative obstacles (Government Perceptions)

A somewhat different perspective has been offered by the analysis of attitudes of the respondents from the public sector towards the role of the state in development of entrepreneurship by providing support to enterprises through the elimination of barriers for the registration and operation of

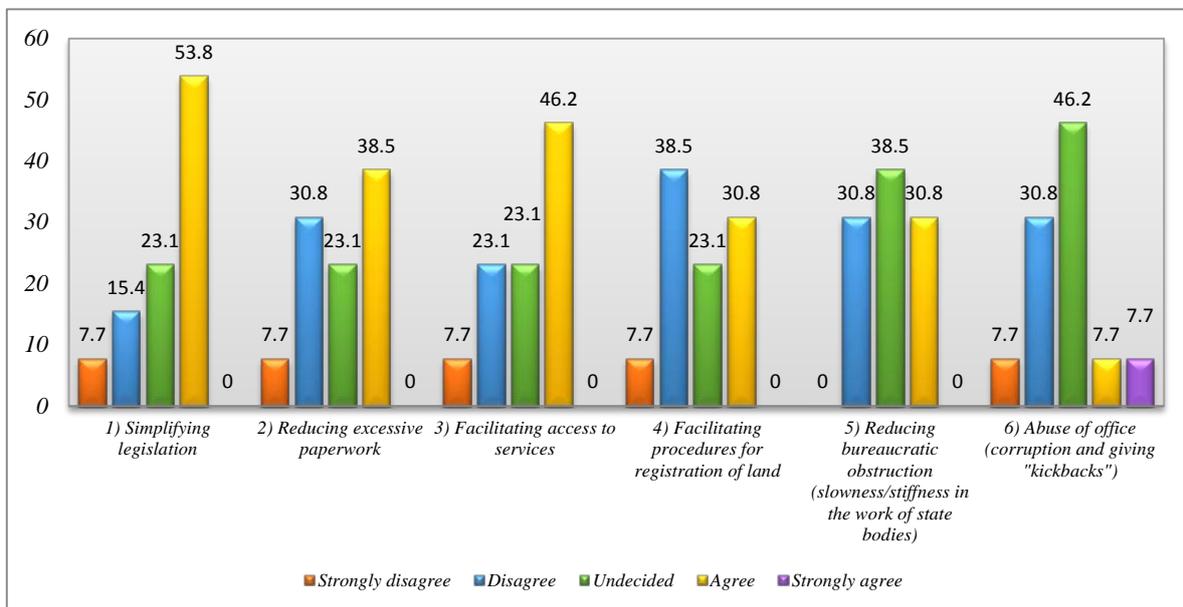


Figure 4.2. Perceptions of public sector about the role of the state in entrepreneurship development

Authors' research

an enterprise.

The respondents from the public sector take the most neutral and positive attitudes regarding the removing of the administrative and regulatory barriers for the registration and operation of an enterprise. Specifically, 46.2% of the respondents expressed a neutral opinion when it comes to the claim "State is working on the reduction of abuse of power (corruption and giving "kickbacks")", while 38.5% of them also had a neutral opinion regarding the claim "State is reducing bureaucratic obstructions (slowness / stiffness in the work of state bodies)". A high percentage of the respondents (53.8%) agree with the claim "State is working on the simplification of legislation", 46.2% of the respondents agree with the claim "State affects the development of entrepreneurship in BiH by facilitating the access to services", 38.5% of them agree with the claim "State is working on the reduction of excessive paperwork necessary for the registration and operation of companies", and 30.8% of the respondents agree with the claim "State actively attempts to facilitate land registration procedures."

4.1.3. Discriminant analysis

Table 4.2. Results of discriminant analysis

F	λ	% Varian ce	Cum. % Var	r_c	Wilk s' λ	χ^2	d f	p
1	0.486	100	100	0.572	0.673	30.871	6	0.001

Authors' research

As can be seen from Table 2 there is a statistically significant difference in the perceptions of the private and state sectors about the role of the state in the development of entrepreneurship through the elimination

of regulatory and administrative barriers to registration and operation of companies at the multivariate level. The existence of a discriminatory function is determined, which is in line with the expectations because the analysis involved two groups based on the activity sector (public and private), whereby the function explains for 100% of intergroup variance. Squared canonical correlation (r_c) indicates that discriminant function explains moderately high 57.2% of the variation within the grouping variable. Wilks' λ discrimination function is moderate (Wilks' $\lambda = 0.673$) and indicates that the discriminatory power of the discriminant function is low. The χ^2 test for function 1 is statistically significant, $\chi^2 = 30.871$, $p = 0.001$. This indicator shows that the discriminative model is significant, meaning that the measures are adequate for distinguishing the identity of the group, but the differences identified are in reality moderate to low.

Table 4.3. Discriminant coefficients and centroids

	Discrimination coefficients	Group	Centroid
Simplifying legislation	0.784	Private sector	-0.297
Reducing bureaucratic obstructions	0.707		
Reducing excessive paperwork	0.662	Public sector	1.597
Facilitating access to services	0.546		
Reducing the abuse of power	0.471		
Facilitating procedures for land registration	0.444		

Authors' research

From the table above one can see the largest identified significant differences between the private and public sectors. At the multivariate level, the biggest difference identified was for the claim "State is working on simplification of legislation" whereby the private sector gives a lower average grade (1.97) than the public sector (3.23). A difference was also registered in the case of the claim "State is reducing bureaucratic obstructions (lowness, rigid functioning of various bodies such as inspection services, institutions dealing with the issuance of various license, certificates, etc.)" The respondents from the private sector provide a lower average evaluation (1.74) of the role of the state than the respondents from the public sector (3.00). Regarding the claim "State works to reduce excessive paperwork (taxes, various certificates, etc.)", the private sector assesses the role of the state as smaller (1.84) than the respondents from the public sector (2.92). The differences were registered in the claim "State facilitates access to services" whereby the private sector considers the role of the state lower (2.09) than the public sector (3.08) as well as in the claim "State works to reduce the abuse of power (corruption and giving "bribe")", with the private sector giving a significantly lower assessment of the role of the state (1.87) than the public sector (2.77). The smallest difference was found for the claim "State actively attempts to facilitate procedures for land registration (in terms of reducing the time limits for the issuance of various approvals, zoning permits, building permits, etc.)". Here again the respondents from the private sector provide a lower average rating (1.94) than the respondents from the public sector (2.77).

It should be noted that although there are differences at the multivariate level between the public and private sectors, with the private sector regularly giving significantly

lower assessment of the state support through removing regulatory and administrative barriers to registration and operation of companies, the above mentioned differences are not extremely large but rather moderate. This is evident from the above average values and Wilks' λ , which indicates that the discriminatory power of the discriminant function is moderate.

5. Conclusions and recommendations

Development and success of enterprises greatly depends on the support provided by the government. Government may create an attractive and easy climate for operations of private subjects, while on the other side, it may also be a great limiting factor in foundation and development of enterprises. It was interesting to examine the role of the state in creating attractive business environment in BiH, and to determine differences in private and public sector perceptions, which was done in this paper. The presented data show that government takes very little action to make the business environment easier for entrepreneurs.

The empirical research confirmed that respondents are not satisfied with the role of the state in eliminating regulatory and administrative obstacles for business. The indicators impose the conclusion that the public sector considers the role of the state in entrepreneurship development as appropriate, but that the private sector considers government tools as bad and insufficient and consequently the role of the state in entrepreneurship development as insufficient. The results confirm research hypothesis that there is a (statistically) significant difference in perception of private and public sectors about the role of the state in entrepreneurship development in terms of administrative and regulatory obstacles.

The general conclusion is that the role of the government in SME and entrepreneurship development is at a very low level in BiH. Therefore, government should invest more efforts in creating a more adequate business climate through provision of better support to enterprises, so that entrepreneurship may better contribute to the overall economic development.

Finally, to business decision makers we suggest the following priorities, directly linked to the development of SMEs: 1. Maintain macroeconomic stability. 2. Increase private investment in the SME sector, 3. Develop the legal framework for the development of entrepreneurship and SMEs, 4. Eliminate administrative and regulatory barriers, and 5. Restructure the economy. From the above priorities for SMEs, we can conclude that our government should make more efforts in order to enhance the institutional framework for SMEs. If those conditions are met, only then can we expect an improvement in the environment for growth, development and operation of SMEs (enabling the introduction of new knowledge and technologies), which would result in keeping the existing and possibly increasing the future number of employees in this sector.

Also, we believe that it is necessary to reach a political agreement and consensus about the transfer of certain competences of SME development from entities to the level of state. In the end, we can recommend the following activities: passing the Law on SMEs in BiH, establishment of Development Agency for SMEs in BiH, establishment of a Credit Guarantee Fund for SMEs at the state level, establishment of the Agency for SME Development in the Federation of BiH. Throughout the paper, it is evident that there are no concrete institutional or legislative reforms aimed at systematic solution for

creating the stimulating environment needed for entrepreneurship development in BiH.

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