



Enabling Environment for Sustainable Enterprises in Serbia



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Foreword

The Serbian Association of Employers is dedicated to strengthening the entrepreneurial position that will contribute to the development of enterprises, further investments and technological modernization, increasing productivity and effectiveness, economic development and export growth, raising the level of education of the population, growth and quality of employment with respect to decent work and environmental preservation, raising standards and quality of life and increasing the overall wealth of society.

Employers' organizations in the region have never been more active in inviting policymakers and national social partners to dialogues to reach understanding and agreement on defining policies and measures aimed at mitigating the consequences of the crisis caused by the COVID-19 pandemic and securing the recovery of the economy. It is high time that participants in economic life in the Republic of Serbia not only understand that the real sector is the basis of development, and the economy of the real sector represents the key start up power that can contribute to a faster recovery from the crisis and a better life, but also act in a coordinated manner for enabling the improvement of the economic environment. The relevant authorities in Serbia need to harmonize their understanding of innovation, both as a process and as a social instrument, with modern trends that exist in advanced economies. Innovation rests on technologies and scientific findings, but it cannot exist outside of economic entrepreneurship. New technologies contribute to the creation of jobs, larger economic growth, social product and export, but what is also very important is that cultivating innovative entrepreneurship in the Republic of Serbia is a way to motivate young people and our best experts to remain in the country, which is necessary for innovations to develop.

The sector of small and medium-sized enterprises could play a big role in the recovery and growth of the Serbian economy, especially having in mind that in the past it has been a very efficient segment of the economy and an important driver of growth and employment, as also shown by the positive experiences of developed European countries. The role the sector will play in the recovery and growth of the Serbian economy will depend above all on the removal, or at least the mitigation of barriers to the revival and further development of this sector's sustainability, among which are insufficient competitiveness, low quality of products, chronic illiquidity, branch and territorial disconnection and difficult access to sources of finance. Also, the success of one part of small and medium-sized enterprises in foreign markets is a clear reflection of the sustainability and systematic capabilities of the sector to produce a competitive product, while continuously improving their market position in competition with other countries.

A stimulating economy based on knowledge requires a very intensive role of the information technology sector, because it represents its infrastructure, so it is necessary to encourage the development of e-business in all areas and to create modern information and telecommunications infrastructure for both national and local governments. Only an economically strong and financially stable Serbia has a chance for long-term growth, job creation, better living standards and greater benefits for all citizens.

The mission of the Serbian Association of Employers is to create a favourable economic environment in which it will be the main generator of economic and social progress, and a critical interlocutor and partner in all decision-making processes of importance for the development of our society and country in general. Strengthening the domestic economy and its competitiveness through modernization and permanent growth is a priority of present and future generations. Following our mission, we have mobilized our strength – the employers of Serbia, and united in the Social and Economic Council, as the highest tripartite body at the national level, with the Government of the Republic of Serbia and representative trade unions, to achieve our vision Strong economy – Strong Serbia!

We firmly believe that our joint achievements will contribute to the harmonious and sustainable development of our economy and strengthen its competitiveness. The present publication discusses the conditions for achieving this goal.

Miloš Nenezić, President of the Serbian Association of Employers

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Acronyms and abbreviations

ACC	Anti-Corruption Council
APC	Agency for the Prevention of Corruption
CIT	Corporate Income Tax
CPC	Commission for Protection of Competition
DAS	Development Agency of Serbia
EESE	Enabling Environment for Sustainable Enterprises
ERP	Economic Reform Programme
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
GRECO	The Group of States against Corruption
HCI	Human Capital Index
HORECA	Hotel, Restaurant, Cafe
ILO	International Labour Organization
MoESTD	Ministry of Education, Science and Technological Development
MSMEs	Micro-, Small and Medium-sized Enterprises
NQFS	National Qualifications Framework of Serbia
PISA	Programme for International Student Assessment
PPS	Public Policy Secretariat
RIA	Regulatory Impact Assessment
SAE	Serbian Association of Employers
SEC	Social and Economic Council
SOE	State-Owned Enterprise
SORS	Statistical Office of the Republic of Serbia
TVET	Technical and Vocational Education and Training
VAT	Value-Added Tax

Executive summary

This report contains an assessment of the status-quo of the Serbian business environment and captures the perception of enterprises on major developmental obstacles, including the effects of the COVID-19 pandemic on the business sector, across six core issues affecting enterprises, as described below.

Good governance

The European Union accession process has created momentum for building a legislative and institutional framework that provides a foundation for good governance. However, the incomplete reform of public administration together with weak rule of law in Serbia have made the application of the framework difficult and hampered the achievement of sound governance. Perceptions of corruption in Serbia are higher than in most aspirational peers in Central and Eastern Europe, and they have been increasing over the past five years. According to Transparency International's 2020 Corruption Perceptions Index, Serbia ranked 94 out of 180 economies. There is low trust in the capacity of public authorities to fight corruption. Almost 60 per cent of EESE survey respondents disagreed completely or partly that existing anti-corruption bodies are effective in addressing complaints made by the private sector. Some 37 per cent of survey respondents admitted that bribery and other forms of corrupt payments were often or occasionally an accepted way of engagement with public servants, especially those representing inspection bodies or when applying for various permits or licences. A particularly critical area that is most prone to corruption is public procurement. Despite significant improvements of the legislative framework, public procurement processes lack credibility and transparency as evidenced by the dwindling number of competitors in public tenders (the average number of bids per tender fell from 3.0 in 2017 to 2.6 in 2020). Moreover, important segments of public procurement are exempted from the general rules by application of exceptional procedures to expedite procurement processes, with such practices having become more frequent during the health crisis.

Social dialogue

Despite a solid institutional infrastructure in place, social dialogue in Serbia is not used at its full potential yet. Although legislation obliges the Government to consult the Social and Economic Council (SEC) on policy initiatives and draft laws falling under its competence, there is a tendency to bypass SEC debates by frequently adopting laws under "emergency procedure". Key ministers are often replaced by deputies within the SEC, which leaves its deliberations and recommendations without full support and authority. Members of parliament are generally unaware of the debates in the SEC and its recommendations. There is no institutionalized mechanism in place for monitoring the follow up action following the SEC's recommendations. The weak commitment of policymakers to tripartite social dialogue limits SEC influence on national policy and law-making processes. An overwhelming majority of EESE respondents (68.2 per cent) found government not very cooperative or completely uncooperative in removing the major barriers to doing business. Tripartite dialogue at the local level is modestly developed with only 24 local social and economic councils established so far. The institutional capacity of tripartite economic and social councils at all levels is rather limited. The secretariats and specialized committees are understaffed and generally lack technical capacity to issue high-quality advice on a wide range of complex economic and social matters. More than a half of survey respondents assessed the activity of SEC at the national level (51.7 per cent) and the local level (55.6 per cent) as ineffective or completely ineffective. The lack of trust in social dialogue institutions undermines the value of collective action and weakens the capacity of employers' and workers' organizations to increase their membership, which translates into limited financial and technical capacity to effectively engage in social dialogue.

Enabling legal and regulatory framework

Over the past two decades, Serbia has made notable progress in reducing the regulatory and administrative burden on businesses, but many challenges remain. Serbia has continuously improved its ease of doing business ranking from 93 in 2013 to 44 in 2020. The share of total administrative expenditure in gross domestic product (GDP) for businesses decreased from 4.07 per cent in 2010 to 3.11 per cent in 2018. Yet, further progress is critical to reduce red tape and improve regulatory transparency and predictability. Only one third of surveyed enterprises found laws and regulations easy to understand and follow, while some 40 per cent agreed only to some extent with the statement and a further one quarter disagreed completely. Micro and small enterprises (27.3 per cent) encounter difficulties more frequently in understanding business regulations compared to medium-sized and large enterprises (10 per cent). Policy changes are too frequent and unpredictable, whereas laws and regulations are often perceived by enterprises as cumbersome, ambiguous and non-transparent due to limited consultations with the business community. This is further exacerbated by an unclear division of competences between various implementation authorities. The lines of accountability between various agencies remain vague, contributing to overlapping functions and unclear reporting lines. The majority of enterprises (66.7 per cent) reported dealing with overlapping regulatory bodies either on a regular basis or occasionally. Tax administration is perceived as a constraint by a near 40 per cent of surveyed enterprises, mainly owing to the high frequency of payments made in a year (33 compared to an average 16.6 across Europe and Central Asia) and time requested to deal with tax payments. Furthermore, enterprises in Serbia still face a high level of payments originating from indirect taxation, with parafiscal charges being the most pressing ones despite efforts to decrease them.

Fair competition

Despite notable progress in the legislative area, Serbia lags behind many peers on international indicators related to market competition. Recently, Serbia ranked 110 out of 141 economies on the indicator for market dominance, which measures the extent to which corporate activity is dominated by a few business groups or is spread across many companies. This also resonates with the perception of the majority of EESE respondents (68 per cent) that anti-trust legislation is ineffective. Furthermore, more progress is needed on levelling the playing field for all enterprises by reducing the size and distortiveness of state aid for privileged state-owned enterprises and large foreign investors and ensuring more transparency in public procurements. State aid is often mistargeted and provides unprofitable state-owned enterprises an unfair advantage over more innovative and competitive domestic private enterprises. Indeed, the continuing large presence and preferential treatment of state-owned enterprises hampers competition in Serbia. Although public companies account for only 19 per cent of value-added and formal employment, they receive 60 per cent of corporate subsidies. In general, state-owned enterprises enjoy preferential treatment in terms of regulatory enforcement too. Foreign investors also benefit from preferential treatment compared to domestic businesses. However, the most significant source of unfair competition stems from the informal sector. More than a third of surveyed enterprises (34.2 per cent) reported that they always or often competed against unregistered or informal businesses. Although the informal economy has been slowly shrinking over the years, the share of informal employment remains high (16.4 per cent in 2020). Facilitating the transition to formality needs to become one of the top priorities of Serbia in the recovery period.

Access to finance

Access to finance is the most significant obstacle to enterprise development in Serbia. Almost half of the EESE survey respondents (48 per cent) found access to finance as a major constraint for the establishment and growth of enterprises. While financial regulations have been significantly improved to enable enterprise lending, financing options for micro, small and medium-sized enterprises (MSMEs) remain weakly diversified. The financial sector in Serbia is dominated by banking loan services while opportunities for non-collateral-based funding remain very limited. There are no thresholds for loans below which collateral requirements are flexible for small businesses, which limits considerably their access to loans. Thus, reliance on loans from commercial banks depends primarily on enterprise size. Alternatives to bank financing have remained either limited or not yet sufficiently regulated to ensure the uptake of non-bank financial instruments (for example, microfinance, factoring, leasing, venture capital, private equity

crowdfunding, and so on), which are particularly valuable for microenterprises, entrepreneurs and start-ups that would otherwise have hardly any access to traditional financing sources. An insignificant proportion of EESE survey respondents (6.7 per cent) assessed the current financial products and services as completely adequate for their needs, while the same was true for only 3.9 per cent of surveyed micro and small enterprises. Weak financial management is another major challenge for micro, small and medium-sized enterprises (MSMEs) to access financing. More than a third of surveyed enterprises (36.4 per cent) highlighted that there was insufficient support targeted at MSMEs to assist them in preparing bankable loan proposals. Furthermore, government support programmes for MSMEs were also found to have unclear eligibility criteria, as well as complicated and non-transparent procedures.

Skills, education and lifelong learning

Skills shortages are becoming an increasingly significant structural obstacle to doing business in Serbia. Over a third of enterprises (33.8 per cent) assessed skills shortages as having a negative or extremely negative impact on enterprise development. Despite recent reforms, including the development of the national qualifications framework, the Serbian education system fails to deliver the skills the labour market needs. This causes a paradox of high enrolment in technical and vocational education and training (TVET) (74 per cent of students enter TVET rather than general education, which is far above the average in the EU of 48 per cent) and solid participation rate in tertiary education (67.2 per cent, which is close to the EU average) contrasted with the significant challenges enterprises face in finding qualified workforce. More than half of surveyed enterprises (53.1 per cent) perceived graduates from vocational and higher education institutions as being only partly prepared or completely unprepared to meet the needs of enterprises as confirmed further by approximately 45 per cent of surveyed enterprises that reported having always or frequent difficulties in recruiting workers with the right skills, especially highly skilled ones. More than half of EESE respondents (54.2 per cent) see the lack of proper coordination among decision-makers, business sector representatives and educational institutions as a major impediment to developing effective education policies and programmes. Serbia lacks an effective skills anticipation and matching system to inform the need for technical and generic skills. With a participation rate below 20 per cent, adult professional development remains low, and life-long learning opportunities underdeveloped.

Introduction

Sustainable enterprises are a principal source of growth, wealth creation and employment, and promoters of innovation and decent work. The development of vibrant, productive and competitive enterprises is, to a large extent, influenced by the environment in which they operate. Getting the enabling environment right is of key importance as enterprises can thrive only in an environment that is conducive to their development and growth.

In 2007 the International Labour Conference adopted conclusions for the promotion of sustainable enterprises¹ and further developed a framework consisting of 17 interconnected and mutually reinforcing conditions² called the Enabling Environment for Sustainable Enterprises (EESE).³ The EESE tool allows stakeholders to assess the environment in which enterprises operate, as well as to formulate evidence-based recommendations and engage with governments to reach shared policy solutions. The evidence collected through the enterprise perception survey serves as basis for informing government decisions and adopting reforms to unlock entrepreneurial potential, support productivity enhancements and boost enterprise performance, which can help to create more and better jobs and generate overall economic growth.

Considering its institutional mandate, the Serbian Association of Employers (SAE) with the technical support of the International Labour Organization (ILO) conducted a comprehensive assessment consisting of a national-wide EESE survey of 450 enterprises to identify key constraints for enterprise development in Serbia. The assessment was finalized and validated in December 2019 and discussions of the key findings and the way forward were planned to take place in 2020.

The process was, however, disrupted by the outbreak of the COVID-19 pandemic, which disproportionately affected enterprises operating in tourism and hospitality, services, transport, manufacturing and trade sectors, with micro and small enterprises being more affected than others. Furthermore, the crisis gave rise to new challenges while exacerbating pre-existing administrative issues and structural challenges, which have played a role in either amplifying the impact of the crisis or limiting the scope of the policy responses to it.

Against this backdrop, the Serbian Association of Employers determined the need to review the previous findings of the EESE survey to take stock and reflect emerging business challenges, needs and priorities arising from the pandemic. This report contains an analysis of the results in six sections, namely: (1) good governance; (2) social dialogue; (3) enabling legal and regulatory framework; (4) fair competition; (5) access to financial services; and (6) education, training and lifelong learning. It synthesizes the key findings of the SAE EESE survey conducted before the pandemic and incorporates additional up-to-date qualitative inputs from enterprises and economic experts with regard to enabling business environment.

1 ILO (2007), Conclusions concerning the promotion of sustainable enterprises, International Labour Conference, www.ilo.org/wcmsp5/groups/public/---ed_emp/--emp_ent/documents/publication/wcms_093970.pdf.

2 The 17 conditions are: (1) peace and stability; (2) good governance; (3) social dialogue; (4) respect for universal human rights and international labour standards; (5) entrepreneurial culture; (6) stable macroeconomic environment and good economic policy of the country (environment); (7) trade and sustainable economic integration; (8) the existence of a legal and regulatory environment; (9) the rule of law and property; (10) fair competition; (11) access to financial services; (12) physical infrastructure; (13) information and communications technology; (14) education, training and lifelong learning; (15) social justice and social involvement; (16) social justice and social inclusion; and (17) responsible environmental management.

3 For more detailed information about EESE Framework visit www.ilo.org/empent/units/boosting-employment-through-small-enterprise-development/eese/lang--en/index.htm.

Survey methodology

In 2019 the Serbian Association of Employers embarked on an ambitious process of assessing the environment in which Serbian enterprises operate. Using the EESE methodology, the 17 conditions were narrowed down to six⁴ through a series of qualitative processes consisting of six focus group discussions with SAE members and 12 in-depth interviews with key informants representing relevant bodies: governmental officials, economic experts and trade unions.

Carried out between May and June 2019, the survey provides the views of 450 enterprises that participated in the interviews. The survey sample reflects the structure of the Serbian economy at the time when the survey was conducted with stratification criteria including enterprise size, sector of operation, region and gender of the respondents (see annex).

The analysis was further complemented with desk research and secondary data from reputable international organizations such as the World Bank, the ILO and others. Where appropriate, national performance was compared to benchmark countries (Austria, Croatia, Hungary and Slovenia), selected based on geographic proximity, similarity of size and performance levels across the 17 EESE conditions.

Given the uneven impact of the COVID-19 pandemic on the business sector, a review of previous findings was conducted to reflect current enterprise perceptions. To that end, the Serbian Association of Employers in collaboration with the Center for Advanced Economic Studies (CEVES) organized three focus group discussions with business representatives to better understand the current enterprise perceptions and needs.

Furthermore, an online questionnaire was administered for focus group participants across all six business conditions. Finally, desk research and secondary data analysis have been updated to reflect changes that have occurred in the legislative, institutional and policy framework since 2019. The analysis was further complemented with views collected through seven in-depth interviews with relevant economic experts.

Limitations

Although the analysis is as comprehensive as possible, there are certain methodological limitations to the study. While the 2021 update aimed to reflect changes in both, the relevant framework and the enterprise perspective (especially considering the impact of the COVID-19 crisis), it could not quantify enterprise views due to excessive survey fatigue at that moment. A number of focus group discussions were held instead. In order to calibrate the enterprise perception, the study used the data collected through other recent studies assessing the impact of the crisis on enterprises.⁵

4 The perception survey focused on six key elements for sustainable enterprises as prioritized by the Serbian Association of Employers following the extensive consultations with its members and other stakeholders, namely: (1) good governance; (2) social dialogue; (3) enabling legal and regulatory framework; (4) fair competition; (5) access to financial services; and (6) education, training and lifelong learning.

5 In particular the report used the data analysis reflected in the following studies: SAE (2021), Navigating the COVID-19 Crisis: Evolving challenges, needs and expectations of Serbian enterprises and CEVES (2021), Enterprises in Serbia and Agenda 2030 – priorities, challenges and the COVID-19 crisis.

1. Good governance

1.1 Overview of legislative, policy and institutional framework

Good governance and efficient public institutions are key drivers of socio-economic development in Serbia and the main prerequisites for joining the European Union (EU). Post-socialist public administration reform in Serbia began in the early 2000s with significant improvements achieved after the adoption of the Public Administration Reform Strategy in 2014. Subsequently, the legislative and institutional framework was improved to ensure a better coordination and alignment of public policies. Among others, a new law on general administrative procedure was adopted in 2016, which gave a strong impetus to changes in public administration work, including through a mechanism for electronic data exchange among public authorities. The law on the planning system was adopted in 2018 to further strengthen the strategic planning system by setting out clear rules for developing, monitoring and reporting on sector strategies. In addition, the civil service legislation was amended in 2018 to specify the rules for merit-based recruitment. The main mechanisms for policy coordination have been put in place and include the Office of the Prime Minister (PMO) and, linked to it, the Public Policy Secretariat (PPS) established in 2014, the General Secretariat of the Government, as well as the Ministry for European Integration, established in 2017. The Public Policy Secretariat plays a key role in carrying out quality control, including on the costing of strategies and their links to medium-term fiscal planning.

The legal and institutional framework of Serbia provides a foundation for good governance. However, the incomplete reform of the public administration together with a weak rule of law have made the application of the framework difficult and hampered the achievement of sound governance. Public administration in Serbia is moderately prepared for accession to the EU. Some progress has been made to improve the efficiency of public institutions through digitalization and the introduction of e-services. However, the structure of the public administration has yet to be streamlined. The lines of accountability between agencies and their parent institutions are not clearly defined, leading to overlapping functions and unclear reporting lines. Political commitment to managerial accountability and systematic delegation of responsibilities is still needed.⁶ Institutions have a bureaucratic and process-oriented approach to planning, budgeting and reporting of their activities. Furthermore, the lack of transparency in, and respect for, the merit-based recruitment procedure provided for under the Serbian legislation for senior civil service positions is an issue of increasingly serious concern.⁷ Contrary to the legal provisions in place on public administration and public enterprise management appointments, the Government continues to fill the positions with 'acting' appointments of indefinite duration. In addition, there have been serious delays in the implementation of the 2016 law on the salary system in the public sector, which introduces the principle of equal pay for equal work for all public sector employees and was aimed to address public administration accountability and meritocracy.

The legal and institutional framework to fight corruption and in relation to economic crime and abuse of office is broadly in place. The planning of anti-corruption policy in Serbia is integrated with its accession negotiations with the EU. The main strategic document is the Action Plan for Negotiations of Chapter 23, originally adopted in 2016 with a revised version approved in July 2020, which foresees actions to be taken by Serbia to advance the accession process, especially in the fields of independent judiciary and the fight against corruption. The national anti-corruption strategy (2013–2018) has expired, and the process for developing a follow-up strategy has not been initiated yet. The law on prevention of corruption was adopted in 2019 to comprehensively cover the anti-corruption area. The most important anti-corruption bodies are the Anti-Corruption Council (ACC) and the Agency for the Prevention of Corruption (formerly the Anti-Corruption Agency). While the Anti-Corruption Council was established in 2001 as an advisory body of the Government to review activities and propose anti-corruption measures,⁸ the Agency for the Prevention of Corruption (APC), which is accountable to the National Assembly, was established in 2010 as

⁶ European Commission (2021), Serbia 2021 Report.

⁷ Ibid.

⁸ Action Plan for Negotiations of Chapter 23, 2020.

an independent state authority with multiple preventative and oversight responsibilities. Among other things, the APC is entitled to initiate and conduct proceedings for the violation of the the law on prevention of corruption, collect the state officials' declarations on their property and income and decide on cases of conflicts of interest. Finally, the Coordination body was established to ensure effective implementation of strategic policy documents in the field of anti-corruption.⁹

Despite the existing institutional infrastructure, there is still no effective coordination mechanism in place to operationalize prevention policy goals and effectively address corruption.

The Anti-Corruption Council is still not operating at full capacity: only 6 out of 13 members have been nominated. The ACC remained active in reporting cases of systemic corruption. In 2019, the ACC published informative reports on enforcement agents, on the lack of transparency as regards signature of contracts by the Government, as well as on public procurement in 2020. However, the Government has not yet started cooperating with the ACC. Furthermore, the number of finalized high-level corruption cases¹⁰ has decreased compared with previous years. Available statistical data on convictions for high-level corruption vary slightly but generally reflect a similar decreasing trend. There were 42 convictions for high-level corruption in the first instance in 2017, 41 in 2018 and 25 in 2019. It should be noted that there is also a decrease in the use of the opinions of the APC on draft laws that are subject to corruption proofing.¹¹ The assessment of legislation is a regular activity of the APC. In 2019, it issued 18 opinions on proposals and draft regulations, most of which have remained unimplemented by the Government without any reasons provided. Positively, the 2020 amendments to the law on prevention of corruption are expected to enhance the independence of the APC and extend its competencies. Yet, shortcomings remain within rules for public officials in terms of their personal business activities, their discretionary right to decide whether to report on parts of their assets, and the low-maximum level of fines for the violation of laws.¹²

A particularly critical area that is most prone to corruption is public procurement. The legal and institutional frameworks of Serbia on public procurement are broadly aligned with the EU acquis.¹³ In December 2019 a new law on public procurement was adopted (which entered into force in July 2020) to further improve public procurement processes. It reduced the administrative procedures for bidders, established an e-portal to facilitate electronic applications and bids and introduced the criterion of the most economically advantageous tender, as well as a special procedure to enhance procurement of innovative goods and services.¹⁴ However, the institutions supervising the process (including the Public Procurement Office, Commission for the Protection of Rights in Public Procurement Procedures, State Audit Institution and Anti-corruption Agency) lack staff capacity and do not always coordinate effectively with the view of fighting corruption in a systematic manner. In February 2020, Serbia adopted a new law on special procedures for linear infrastructure projects, which allows the Government to exempt linear infrastructure projects of "special importance for the Republic of Serbia" from the application of public procurement rules. National public procurement legislation can be suspended for entire or particular phases of a project and the Government is empowered to select a strategic partner in circumstances deemed as urgent. This new law undermines the added value and effective implementation of the new law on public procurement.¹⁵ The response to the

9 The Coordination Body, as envisaged by Action Plan for Negotiations of Chapter 23, is supposed to be headed by the Prime Minister and Minister for Justice and convene the ministers for the interior, finance, education, public administration and local self-government and health. This body is supposed to monitor work of three implementation groups, each responsible for separate area and convening representatives of main institutions relevant for that area.

10 OECD (2021), Competitiveness in South East Europe: A policy outlook. High-level corruption is not defined explicitly but the anti-corruption remit of these bodies but comprises abuse of official authority, trading in influence, and passive and active bribery when the defendant or the person to whom a bribe is given is an official or responsible person performing a public function on the basis of election, appointment or appointment by the National Assembly, the President, the Government, the general session of the Supreme Court of Cassation, the High Judicial Council or the State Prosecutorial Council. The Prosecutor's Office for Organized Crime and the Section for Suppressing High-Level Corruption within the Service for Combating Organized Crime of the Criminal Police Directorate have responsibility for the investigation and prosecution of high-level corruption.

11 Corruption proofing of legislation has a firm legal ground in the law on prevention of corruption. State administration bodies are obliged to submit draft laws in areas of high risk and areas affected by international agreements in the anti-corruption field to the Agency for the Prevention of Corruption to obtain its opinion.

12 Council of Europe/GRECO (2020), Second Compliance Report Serbia.

13 European Commission (2021), Serbia 2021 Report.

14 SAE (2020), Počinje primena Zakona o javnim nabavkama, <https://www.poslodavci.rs/pocinje-primena-zakona-o-javnim-nabavkama/>

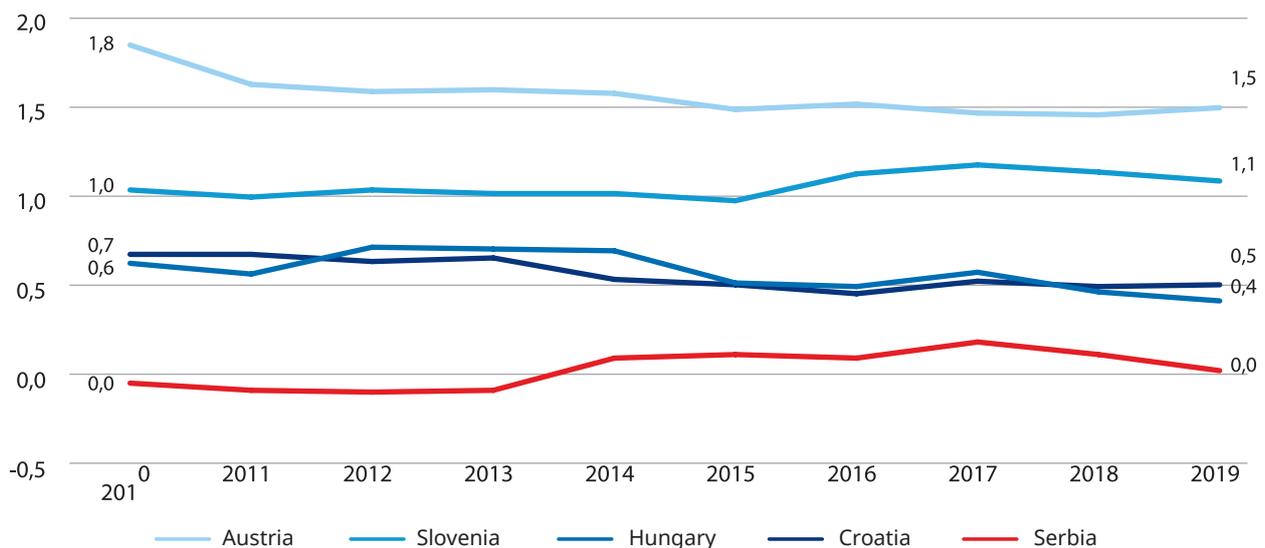
15 European Commission (2021), Serbia 2021 Report.

COVID-19 crisis enabled the use of exceptional procedures to expedite procurement processes. Overall, the level of competition in the public procurement process remains limited: the average number of bids per tender fell from 3.0 in 2017 to 2.6 in 2020. Competition is even lower at the local level: there was an average 2.1 bids for tenders published by local public administrations in 2018.¹⁶

1.2 Government effectiveness

There is a low confidence in the effectiveness of government in Serbia. The indicator “government effectiveness” measures the quality of public services, the capacity of the civil service and its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the Government’s commitment to such policies. It is measured on a scale from approximately -2.5 to 2.5, where higher values correspond to better governance. With an average value around zero, Serbia performed the worst among the reference countries (Figure 1). Although a slight improvement in the index is evidenced in the period 2014–2016, a decline is noticeable since 2017. Austria is the best performer among the reference countries, with an average score of 1.6, while Croatia and Hungary had the second lowest average scores, at 0.61 and 0.6 respectively.

Figure 1. Government effectiveness



Source: World Bank databank, Worldwide Governance Indicators.

The response to COVID-19 reflected the limited capacity of the Government of Serbia to design and implement efficient and well-targeted economic support measures. Serbia implemented the largest fiscal support package in the region to counter the impact of the crisis. The package included a wide range of measures to support enterprises including the deferment of labour tax and contribution payments as well as corporate income tax payments, wage subsidies and a moratorium on enforcement and interest on tax debt. Serbia also introduced a state guarantee scheme for banks that lend to small and medium-sized enterprises (SMEs) in order to support their liquidity. The generous economic support measures were critical to preventing significant economic consequences, especially for labour market outcomes, but it has resulted in a significant narrowing of the fiscal space.¹⁷ Moreover, the Government of Serbia has implemented a relatively narrow set of responses, which did not distinguish between enterprises by sector or their financial and operational health. The one-size-fits-all approach (namely allowing MSMEs to apply for economic support measures, provided that they did not lay off more than 10 per cent of their employees for the duration of the wage subsidy transfer and three subsequent months) led to the provi-

¹⁶ World Bank Group (2020), Serbia Systematic Country Diagnostic Update.

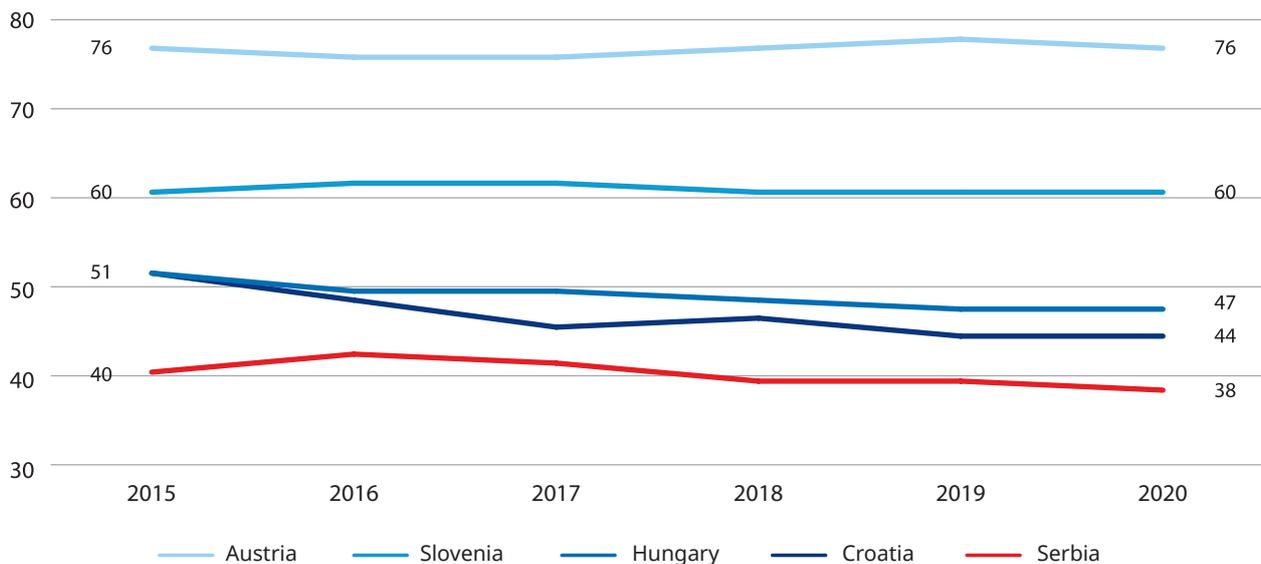
¹⁷ OECD (2021), Competitiveness in South East Europe: A Policy Outlook.

sion of assistance to some enterprises that would have been sustainable without support, while the most affected enterprises struggled to stay afloat. Available analysis shows that resources spent on enterprises that did not need assistance could have sustained enterprises in the most affected sectors (tourism and hospitality, personal services) for some 12 months.¹⁸ Only the third support package brought long-awaited sector-specific measures (such as direct aid towards city hotels, tourism agencies, car rental and passenger transportation enterprises) and it included some measures for large enterprises.¹⁹

1.3 Perception of corruption

Despite existing anti-corruption measures and institutions established to combat it, corruption remains a major issue in Serbia. The Corruption Perception Index, created by Transparency International, measures the perceived levels of public-sector corruption as seen by businesses and analysts in a given country. It is a composite index, drawing on different expert and business surveys, where 0 is highly corrupt and 100 is highly clean. In comparison to Croatia, Hungary, Austria, and Slovenia, which ranged between 44 and 76, Serbia had an average score of 39.8 throughout the period 2015–2020 (Figure 2). After a short-lived improvement in 2016, Serbia declined to 38, its lowest level since 2012. In 2020 Serbia ranked 94 out of 180 economies. Focus group discussions confirmed the perception of corruption. As much as 65 per cent of participants partly agreed that they often come across corrupt practices when performing regular operations, while 85 per cent agreed or partly agreed that corruption is an issue significantly affecting their business.

Figure 2. Corruption Perception Index



Source: Transparency International.

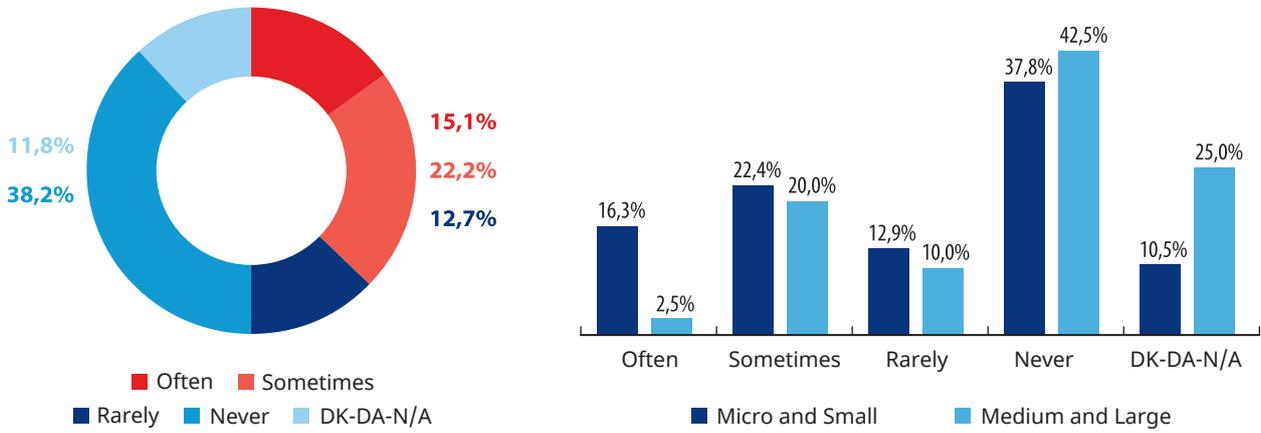
Bribery and other forms of corrupt payments are perceived as impacting consistently on enterprises, with small business being more affected than the large ones. The EESE respondents (37.3 per cent) admitted that bribery and other forms of corrupt payments were often or occasionally an accepted way of engagement with public servants, which was an issue for them, while a further 12.7 per cent reported that such cases may occur only rarely (Chart 1). Some 38.2 per cent believed that enterprises did not engage in corrupt practices. Furthermore, corrupt practices are particularly burdensome for micro and small enterprises. While 16.3 per cent of respondents from micro and small enterprises reported that corrupt payments were often an issue, only 2.5 per cent of respondents from medium-sized and large enterprises agreed with this statement. Moreover, some differences were noticed

¹⁸ CEVES/World Bank (2020), The COVID-19 Crisis and Serbia's SMEs: Assessment of Impact and Outline of Future Scenarios.

¹⁹ SAE (2021), Navigating the COVID-19 Crisis: Evolving challenges, needs and expectations of Serbian enterprises. Second edition.

depending on the respondents' gender. Significantly more women (36.1 per cent) than men (18.0 per cent) believed that corrupt payments were often or sometimes an issue that affected enterprises.

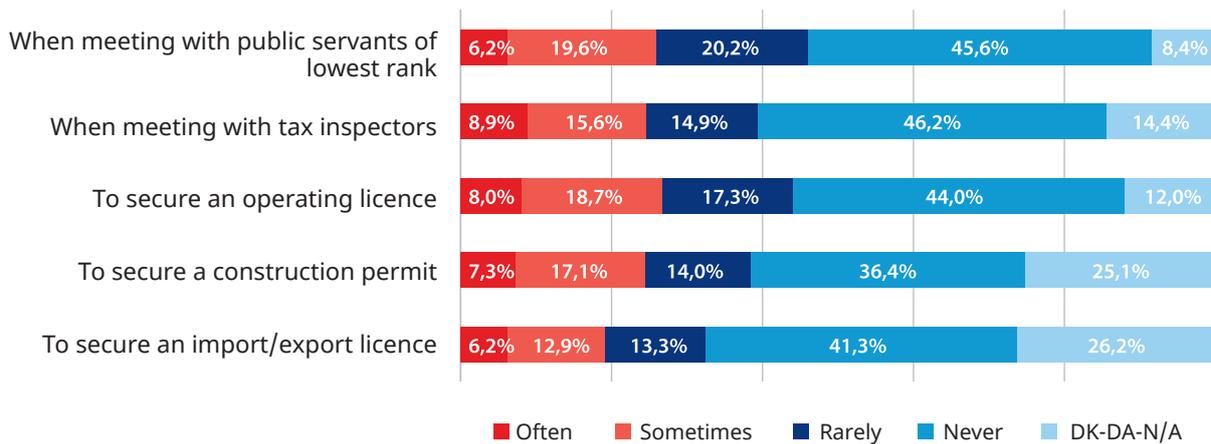
Chart 1. Are bribery and other forms of corrupt payments an issue that consistently affects enterprises? All enterprises (left) and enterprises by size (right)



Source: Transparency International.

Monetary compensation is often or occasionally expected from enterprises when interacting with various public institutions and inspectors. Approximately a quarter of respondents believed that compensation was expected when dealing with public servants or tax inspectors, as well as when securing an operating licence or construction permit, while approximately a fifth reported that compensation was expected to secure import/export licences (Chart 2).

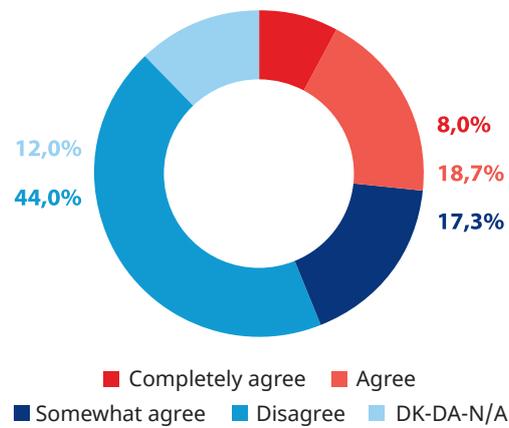
Chart 2. Are enterprises expected to give monetary compensations/gifts?



Source: EESE survey.

Enterprises were divided when asked whether the only way to avoid administrative obstacles is by making extra 'speed' payments or illicit 'backhanders'. Specifically, more than a quarter (25.7 per cent) agreed completely this was the case and a further 17.3 per cent agreed to some extent (Chart 3). However, a significant share of respondents disagreed (44 per cent). It should be noted that focus group participants were reluctant to openly discuss corruption. It can only be assumed that it was the concern about backfiring rather than unwillingness to talk or lack of interest in the topic that prevented participants from addressing the issue in more depth.

Chart 3. To what extent do you agree with the statement ‘the only way to avoid administrative obstacles is by making extra ‘speed’ payments or illicit ‘backhanders’?

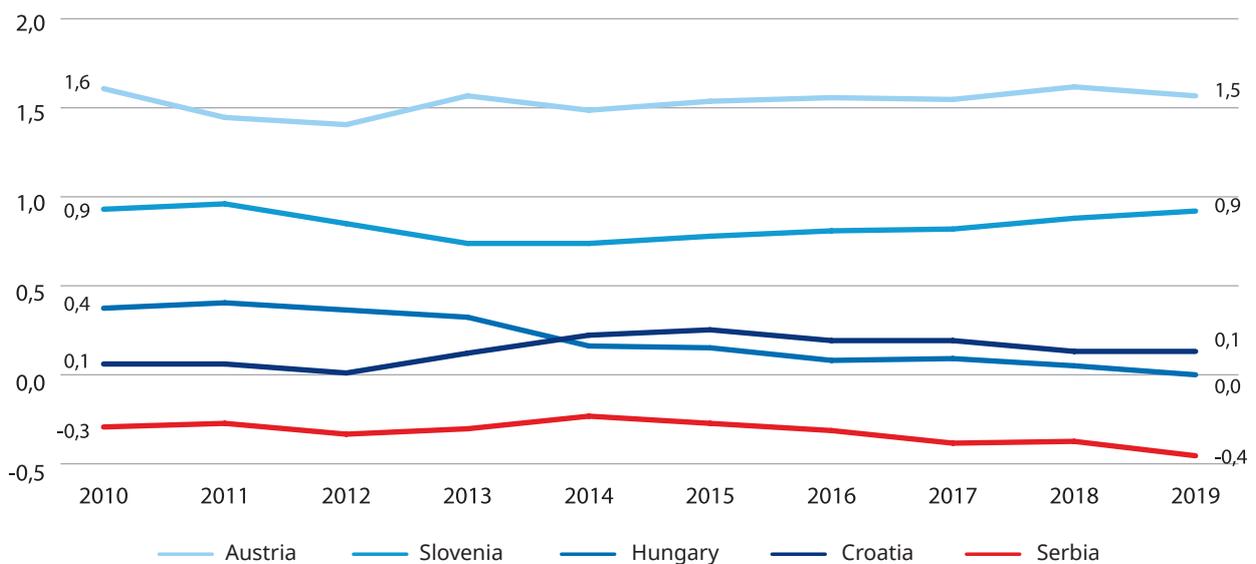


Source: EESE survey.

1.4 Control of corruption

Public administration institutions are perceived as incapable of protecting public interest from the abuse of power for private gain. According to the Control of Corruption Index, that measures the extent to which public power is exercised for private gain on a scale from -2.5 to 2.5, Serbia stands substantially lower than the reference countries (Figure 3). Austria was the best performer with an average score of 1.6 and the second lowest was Hungary with an average of 0.2. Serbia had an average around -0.3 throughout 2010–2019. There was some improvement in 2013–2014 amid the second wave of public administration reform, followed by a decline to its lowest level in 2019 (-0.4).

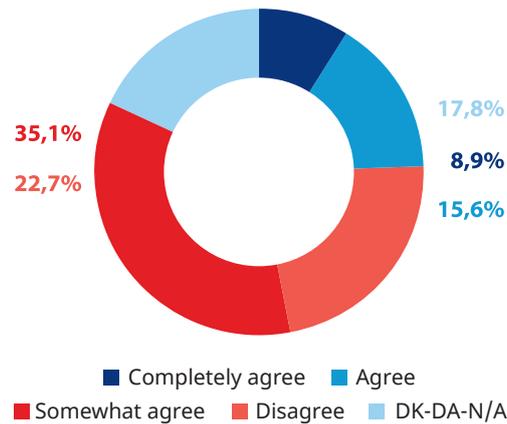
Figure 3. Control of Corruption Index



Source: World Bank databank, Worldwide Governance Indicators.

The EESE survey confirmed the ineffectiveness of public authorities to fight corruption. When asked whether effective, independent anti-corruption institutions exist to handle complaints made by the private sector, 57.8 per cent of respondents disagreed completely or partly with the statement (Chart 4). Almost a quarter of respondents (24.5 per cent), however, believed that the anti-corruption bodies were dealing effectively with complaints made by enterprises.

Chart 4. Do effective, independent anti-corruption institutions exist to handle complaints made by the private sector?



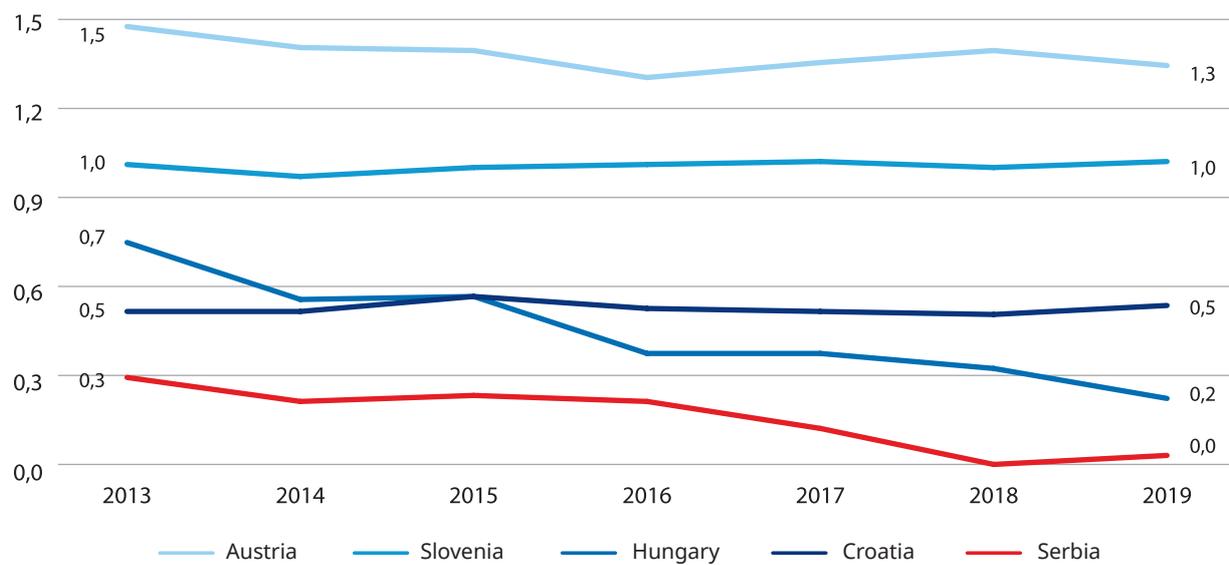
Source: EESE survey.

1.5 Participation in governance processes

The “voice and accountability” index illustrates that the perception of public political participation and freedoms in Serbia has been low²⁰ and deteriorating throughout the years. This indicator measures perceptions of the extent to which a country’s citizens can participate in selecting their government, as well as freedoms of expression, association and a free media on a scale from -2.5 to 2.5 with higher values indicating better governance. In Serbia, the average score of 0.1 throughout the period 2013–2019 was substantially lower compared to the reference countries, which ranged between 0.4 and 1.3 (Figure 4). Electoral legislation largely corresponds to international standards and citizens enjoy a significant degree of freedom to make political decisions. Yet, the electoral management is often non-transparent, and implementation of existing rules is flawed in some respects. Furthermore, as repeatedly indicated by observers of the democratic processes, the overall political environment in Serbia is not conducive to the exercise of freedom of expression.²¹

²⁰ Data for Serbia are available since 1996. The average value for Serbia from 1996–2019 was -0.02 points with a minimum of -1.22 points in 1996 and a maximum of 0.34 points in 2009.

²¹ Freedom House Profile Serbia (2020), Human Rights Watch Serbia.

Figure 4. Voice and accountability


Source: World Bank databank, Worldwide Governance Indicators.

2. Social dialogue

2.1 Overview of legislative, institutional and policy framework

Serbia has a relatively wide institutional infrastructure in place for social dialogue.²² The legal foundation of social dialogue is set out in the labour law of 2005,²³ which envisages the establishment of employers' associations and trade unions as well as the method of and requirements for determining their representativeness. The development of institutionalized tripartite social dialogue was initiated after the democratic changes in Serbia in 2000, which was supported by the ratification of ILO core conventions in the area of industrial relations.²⁴ The Social and Economic Council (SEC) of Serbia was established initially by a tripartite agreement in 2011. Currently, the law on social and economic council of 2004, as amended in 2008, is the legal base for the functioning of the SEC. The mandate of SEC is sufficiently broad to address and debate a wide range of economic, social and labour matters. Its current membership includes six representatives of line ministries, six representatives of the Serbian Association of Employers (SAE) and six trade union representatives (four from the Confederation of Autonomous Trade Unions of Serbia (CATUS) and two from the Trade Union Confederation NEZAVISNOST. Four specialized standing committees²⁵ are operational within the SEC consisting of four members each – one from each representative social partner. Apart from the SEC established at the national level, there are 24 social and economic councils at the level of the autonomous territories and the local government.

Despite the significant progress made in institution building,²⁶ the effectiveness of social dialogue remains limited. Although the legislation obliges the Government to seek the opinion or recommendation of SEC on draft laws and policies falling under its competence, the Government has shown a tendency to circumvent the SEC debates by frequently adopting laws under "emergency procedure",²⁷ with this practice seeing an increase after the outbreak of COVID-19 crisis. On a different but related note, the short deadlines given for debating and issuing recommendations and opinions on a bill often make the discussion and its outcome meaningless.²⁸ Moreover, consultations are held at a late stage of policymaking. The social partners are not involved in the tripartite working groups on drafting bills with concerned ministries and are rarely aware of the goals and content of the legal and policy initiatives of the Government. While the SEC recommendations and opinions are adopted by consensus, the required quorum is low, which risks delegitimizing the process and the quality of its outcomes.²⁹ In addition, ministers are often replaced by deputies within the SEC, which leaves its deliberations and conclusions without full support and authority. Furthermore, members of parliament are generally not aware of the debates in the SEC nor of its recommendations. Finally, yet importantly, the SEC budget is low which keeps its institutional capacities rather limited.

22 Social dialogue is defined by the ILO to include all types of negotiation, consultation or simply exchange of information between, or among, representatives of governments, employers and workers, on issues of common interest relating to economic and social policy. It can exist as a tripartite process, with the government as an official party to the dialogue or it may consist of bipartite relations only between labour and management (or trade unions and employers' organizations), with or without indirect government involvement.

23 The Labour Law was partially amended in 2014, 2017 and 2018 but further progress on Labour law reform is a condition for advancing the EU accession agenda.

24 Serbia has ratified 77 ILO conventions, of which 62 are in force, including the eight fundamental and four governance conventions. The Labour Relations (Public Service) Convention, 1978 (No. 151) and Collective Bargaining Convention, 1981 (No. 154) have not been ratified yet. See www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:11200:0::NO::P11200_COUNTRY_ID:102839.

25 The standing committees cover the following areas: legislation, collective bargaining and labour dispute resolution, economic issues, and occupational health and safety

26 The functioning of SEC has seen some improvements over the past decade. Sessions of the SEC have become more regular and discussions more meaningful. Furthermore, important strategic documents were brought for discussion within SEC, such as the Economic Reform Programme and matters pertaining to negotiations in EU accession process, in particular action plan for Chapter 19, among others.

27 ILO (2017), Report on Peer Review of the Economic and Social Councils in the Western Balkans. For example, in 2017, 60 per cent of laws relevant to business did not go through a public hearing, 90 per cent were made by urgent procedure and half of all draft laws were not available on the relevant ministry websites.

28 Ibid. More than that the procedures for submission of SEC recommendations are lengthy and bureaucratic. The opinion should first be submitted to the initiating ministry, and only after 30 days with no reply can be sent directly to the government.

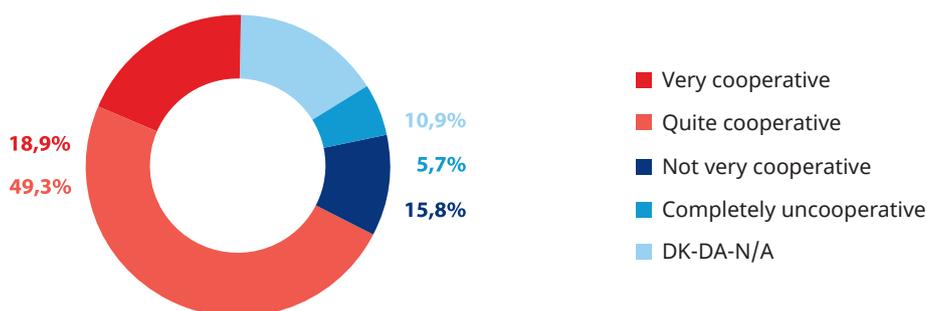
29 Ibid.

Employers' and workers' organizations in Serbia face significant capacity challenges that prevent them from engaging more effectively in social dialogue. Both social partners look back at a relatively short history as independent membership organizations. Moreover, unlike the trade unions, which existed in the former socialist system, employers' organizations emerged after the transition to a market economy as a new, previously non-existent social actor. The Serbian Association of Employers represents approximately 30 per cent of all registered businesses in Serbia³⁰, yet its membership needs to be further increased in a number of economic sectors and industries. It should be noted that many enterprises are still not aware of the benefits of collective action and are hesitant to join employers' organizations. Social dialogue, including collective bargaining, is also strongly affected by the dynamics of reform of the labour legislation, including the provisions on registration and representativeness of trade unions and employers' organizations.³¹ The increase of thresholds for representativeness at the branch level from 30 per cent to 50 per cent as a pre-condition for the extension of collective agreements³² significantly reduced the number of collective agreements in the private sector.³³ Lack of strong political will to involve social partners in policymaking undermines the value of collective action and weakens the capacity of employers' and workers' organizations to increase their membership. In 2018, trade unions (CATUS and NEZAVISNOST) and the Serbian Association of Employers submitted their observations to the ILO Committee on the Application of Standards on the implementation of Convention No. 144 on Tripartite Consultations.³⁴

2.2 Effectiveness of social dialogue

The EESE survey confirms the ineffectiveness of social dialogue. An overwhelming majority of EESE respondents (68.2 per cent) found government not very cooperative or completely uncooperative in removing the major barriers to doing business (Chart 5). Although Serbia has set up a regulatory and institutional framework for effective and inclusive policymaking, authorities still fail to engage employers consistently in policy developments relevant to them. Focus group participants highlighted the lack of timely and regular consultation in the process of drafting legislation and the frequent use of urgent procedures for adopting legislation.³⁵ Despite good progress achieved in reducing administrative and regulatory burdens for businesses, policy changes are too frequent and unpredictable, which adversely affects enterprise operations.

Chart 5. How cooperative is the government with employers' organisations in removing the major barriers to doing business?



Source: EESE survey.

30 SAE data.

31 Decent Work Country Programme for Serbia, 2019–2022.

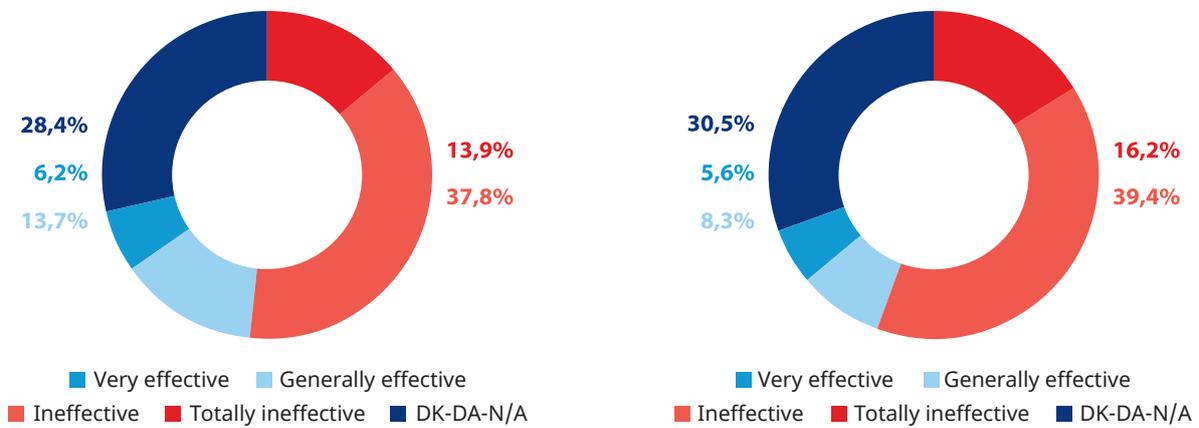
32 Even though the Labour Law envisages the extension of collective agreements (branch and general), the 2014 amendments increased the threshold for representativeness at the branch level from 30 per cent to 50 per cent, which in practice is almost impossible to achieve.

33 Currently, there are 11 sectoral collective agreements in the public sector and 2 sectoral collective agreements in the private sector.

34 According to the social partners, in practice social dialogue was reduced to the strict minimum at all levels in Serbia. Draft legislation on social and labour issues was not always submitted to the SEC and consultations with social partners were held too late, or not at all. The Government was called upon to take the necessary and appropriate measures to ensure effective and efficient tripartite consultation of the national social partners in implementation of Convention No. 144. https://www.ilo.org/dyn/normlex/en/f?p=1000:13101:0::NO:13101:P13101_COMMENT_ID:3953293

In addition, EESE respondents perceive social dialogue institutions as rather ineffective. More than half of respondents (51.7 per cent) assessed the activity of SEC at the national level as ineffective or completely ineffective (Chart 6). Focus group participants were further asked to evaluate SEC influence on creating an enabling business environment. The majority of participants (68 per cent) gave it a rating of 2 on a scale from 0 to 5.³⁶ Similarly, the activity of local SECs was perceived as ineffective or completely ineffective by 55.6 per cent of respondents. Moreover, it appears that many focus group participants (55 per cent) were not even aware whether a local social and economic council existed or not in their municipality. Only 10 per cent noted that a local social and economic council was established and that they were consulted a couple of times. Focus group participants confirmed further that social and economic councils (at both national and local levels) have low visibility and limited influence on policy and law making. In their view, the main reason is the lack of commitment of authorities to engage in tripartite social dialogue. In addition, it was highlighted that the technical capacities of these institutions were also limited and that they cannot deliver high quality policy input and expertise. Focus group participants also admitted that employers need to build stronger organizations at local levels to be able to have a greater policy influence.

Chart 6. How effective are the social and economic councils at national (left) and local (right) levels?



Source: EESE survey.

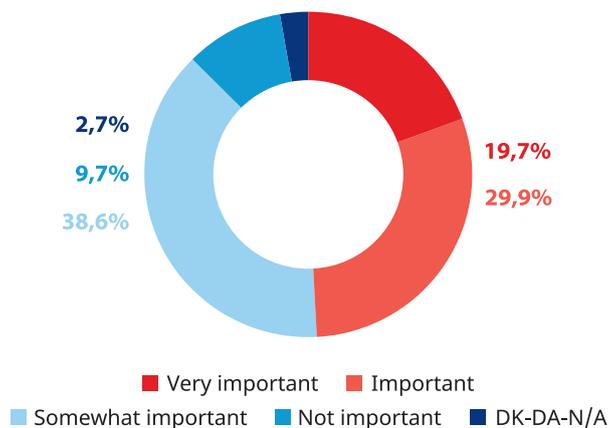
2.3 Workplace cooperation

Employers recognize the role that workplace cooperation³⁷ may have in the development of their enterprises. Precisely, nearly half of respondents (49.6 per cent) find workplace cooperation as important or very important, and a further 38.6 per cent see it as somewhat important in achieving greater business performance (Chart 7). A large proportion of employers are becoming increasingly aware, as confirmed during focus group discussions, that workplace cooperation can increase enterprise productivity, efficiency and competitiveness and lead to more job satisfaction, better working conditions and motivating wages for employees. However, employers had divergent views on the need to consult employees when taking important business decisions. While 55 per cent confirmed that they consult employees when making an important decision (at least in some instances), 45 per cent of respondents revealed the opposite practice.

³⁵ According to statistics from the Public Policy Secretariat, consultations were conducted for 15 out of 42 relevant draft laws (35.71 per cent) during 2020.

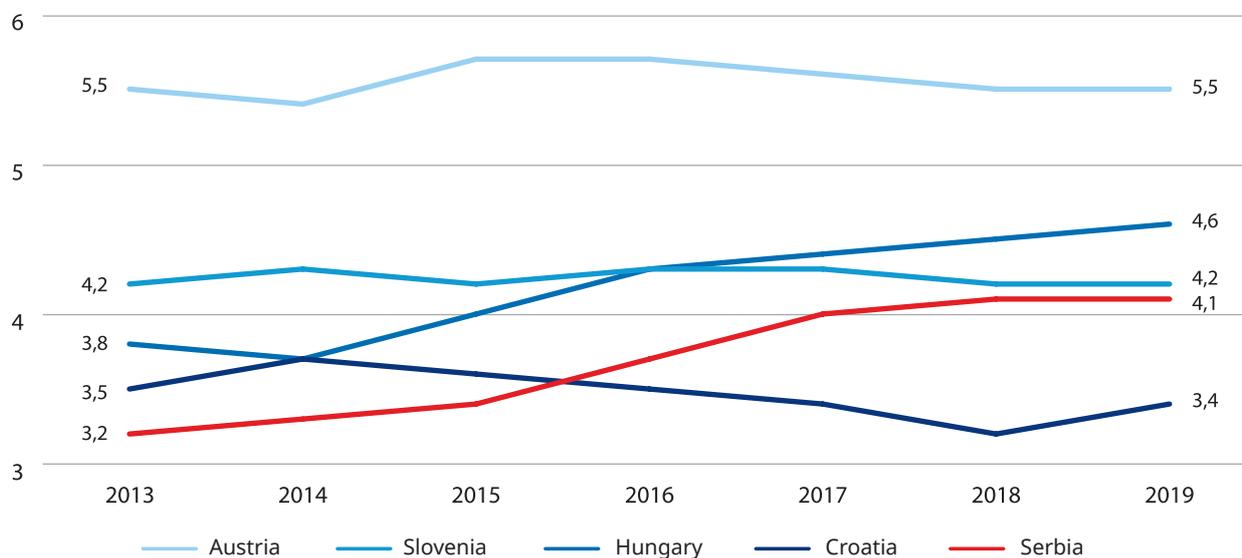
³⁶ Focus group participants assessed the influence of SEC on a scale from 0 to 5, with 0 being the lowest value and 5 being the highest value respectively.

³⁷ According to the ILO, workplace cooperation can take various forms, such as information sharing, direct or indirect consultation, and financial participation. Collective bargaining is also a form of and a vehicle for workplace cooperation.

Chart 7. Does workplace cooperation have an important role in the development of enterprises?

Source: EESE survey.

Indeed, the cooperation between employers and workers has been improving over time. The indicator “Cooperation in Labour-Employer Relations” measures labour-employer relations on a scale from 1 to 7, with higher values indicating more cooperation. According to this indicator, Serbia has gradually improved its performance in the period between 2013 and 2019, ultimately performing better than Croatia, at 4.1 in 2019 (Figure 5). The best performing country with an average value of 5.6 was Austria.

Figure 5. Cooperation in Labour-Employer Relations

Source: World Economic Forum, Executive Opinion Survey.

3. Enabling legal and regulatory framework

3.1 Overview of legislative, institutional and policy framework

In the early 2000s Serbia embarked on a regulatory reform process but notable progress was accomplished with the establishment of the Public Policy Secretariat as part of the public administration reform in 2014.

In the early years, the regulatory reform was partial. In 2003, the Serbian Business Regulation Reform Council was established as an ad hoc body of the Government tasked with supervision and promotion of the regulatory reform and monitoring of private sector development. In 2004, the Regulatory Impact Assessments (RIAs) were first introduced, as one of the most important regulatory quality tools. In 2008, the Regulatory Reform Strategy³⁸ was adopted followed by the set-up of supporting institutional infrastructure. The Comprehensive Regulatory Reform Unit was established in 2008, tasked with carrying out a “regulatory guillotine”³⁹ and developing recommendations to improve the business environment, while the Business Regulation Reform Council continued drafting opinions of RIAs. In 2010, the Office of Regulatory Reform and Regulatory Impact Assessment was set up as a permanent public administration authority providing professional service to the Government. In 2014, the Public Policy Secretariat was established taking over the mandate of the Regulatory Reform and Regulatory Impact Assessment Unit and was additionally charged with coordinating the mutual alignment of the Government’s strategic documents. Apart from providing opinions of legislative bills and RIAs appended to them, the National Public Policy Secretariat was also tasked with issuing opinions of the Government’s draft strategic documents.

While the main mechanisms for policy coordination are largely in place, further progress is critical to improve the quality of business regulations and consistency in their implementation. Reform measures undertaken so far resulted in a reduced administrative and regulatory burden for businesses. The share of total administrative expenditure in gross domestic product (GDP) for businesses decreased from 4.07 per cent in 2010 to 3.11 per cent in 2018.⁴⁰ Yet, policy changes are too frequent and unpredictable whereas laws and regulations are often perceived as too cumbersome and non-transparent due to limited consultations with the business community ahead of regulatory changes.⁴¹ Government decisions in a number of business-relevant areas are often taken without proper consultation with businesses and social partners, and they are taken under time constraints that do not allow businesses to organize and adapt their operations to new rules in good time. Furthermore, the legislative changes adopted as part of the EU accession process are not consistent. Among other things, the adoption of secondary legislation that guides the operational enactment of primary legislation usually comes with substantial delays or does not come at all. This is further exacerbated by an unclear division of competences and reporting lines between various implementation authorities.

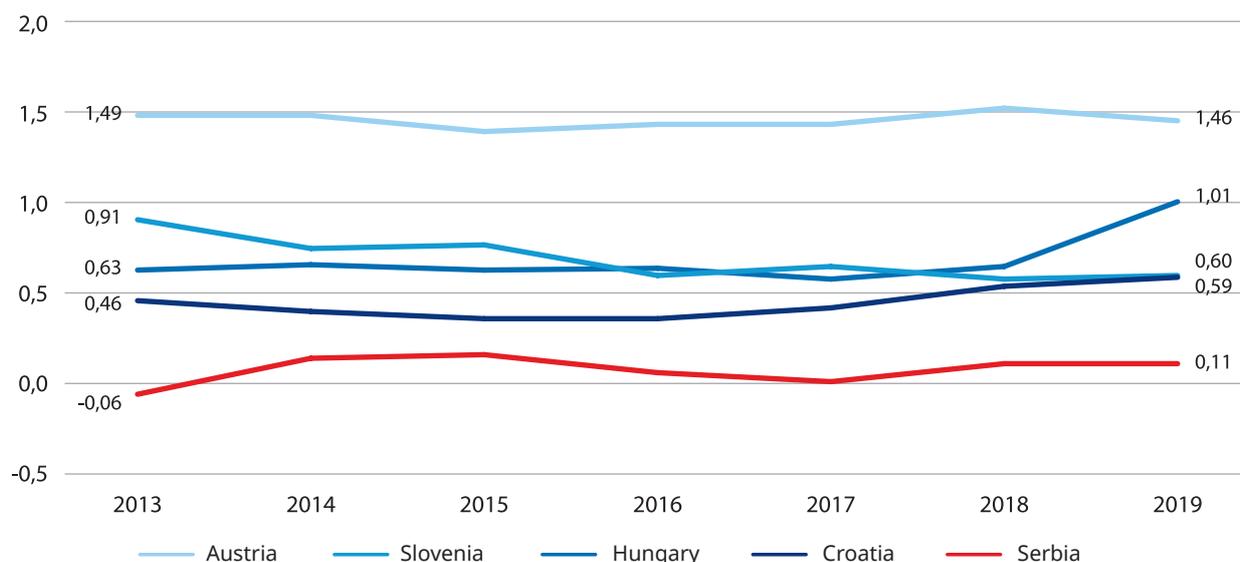
The World Bank Regulatory Quality Index confirms the need to further improve the business regulatory framework. This indicator measures the ability of the Government to provide sound policies and regulations that enable and promote private sector development. The estimate of governance is measured on a scale from -2.5 to 2.5, where higher values correspond to better governance. With an average value around 0.01 in the period from 2013 to 2019, Serbia had the lowest score among the reference countries (Figure 6).⁴²

38 The Regulatory Reform Strategy was aimed at establishing a regulatory system which: (i) promotes economic development and social prosperity; (ii) supports national competitiveness, protecting public interest at the same time; (iii) reduces administrative business costs; (iv) accelerates and reduces administrative procedures, and (v) improves the international rating of the Republic of Serbia in terms of business and investment environment quality. The implementation of the Strategy improved the Serbian legal and regulatory framework, mainly through the repeal of redundant legislation and a decrease in the administrative burden imposed by regulations on businesses.

39 The regulatory guillotine is an orderly, systematic, transparent, rapid and low-cost means of reviewing a large number of regulations against clear criteria and eliminating those that are no longer needed.

40 Government of the Republic of Serbia (2020), Economic Reform Programme for the period 2021-2023.

41 World Bank Group (2020), Serbia Systematic Country Diagnostic Update.

Figure 6. Regulatory Quality Index

Source: World Bank databank, Worldwide Governance Indicators.

3.2 Ease of doing business

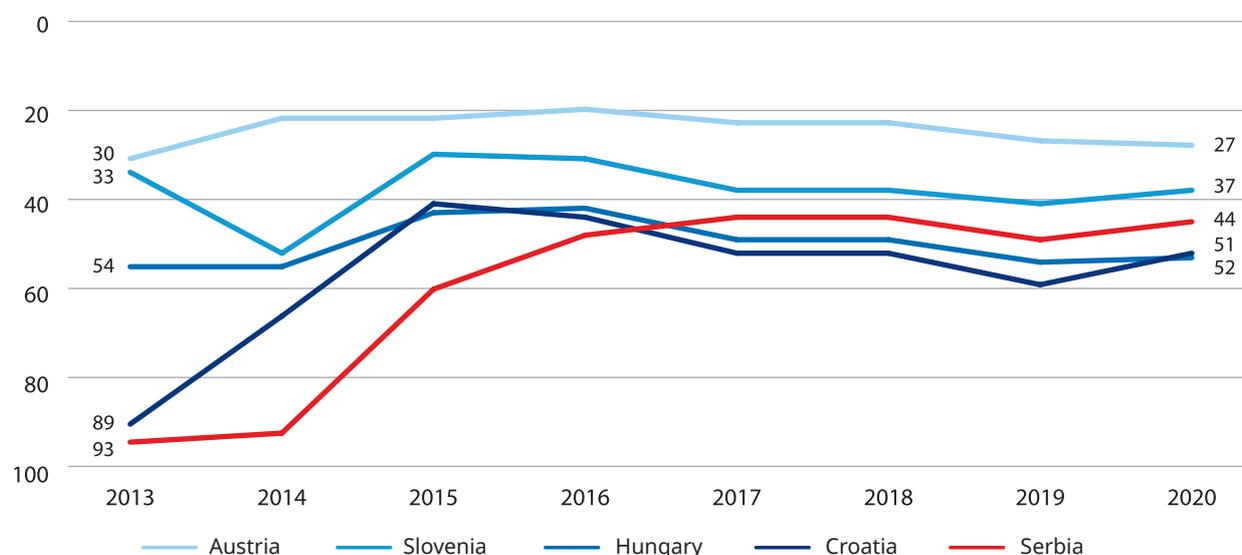
As a result of reforms implemented, Serbia has continuously improved its ease of doing business ranking from 93 in 2013 to 44 in 2020. The World Bank Ease of Doing Business Index ranks economies from 1 to 190 (in 2020), with first place being the best. A high ranking corresponds to the regulatory environment being assessed as conducive to business operations. This index averages the country's percentile rankings on ten indicators with equal weight given to each.⁴³ At the beginning of the reference period Serbia was ranked the lowest (93) relative to the reference countries, but by the end of 2020 Serbia had considerably improved its score (44) and surpassed Hungary (52) and Croatia (51) (Figure 7). It should be noted, however, that the rapid increase in the ranking of Serbia in the period 2014–2016 was due not only to improvements within the national regulatory framework but also to methodology changes in the Doing Business Index ranking.

Significant improvements have been achieved in dealing with construction permits, whereas progress on other indicators has been modest or non-existent. Precisely, the good score (ninth position) recorded in dealing with construction permits is due to the supportive measures introduced in the past years. In 2019, Serbia reduced the time needed to obtain a construction permit by introducing an electronic application system. In 2017 Serbia made dealing with construction permits faster by implementing an online system and streamlining the process of obtaining technical conditions for the construction permit, while in 2016 Serbia made dealing with construction permits less costly by eliminating the land development tax for warehouses and it also introduced a mandatory inspection of foundation works. A solid contribution to good results in Serbia was also provided by the reforms abolishing the obligatory use of seals by businesses, easing the real estate registration, improving the insolvency procedure and minority shareholders' rights. On the negative side, enterprises still encounter major difficulties when starting a business, getting electricity, paying taxes and getting credit (Figure 8).⁴⁴

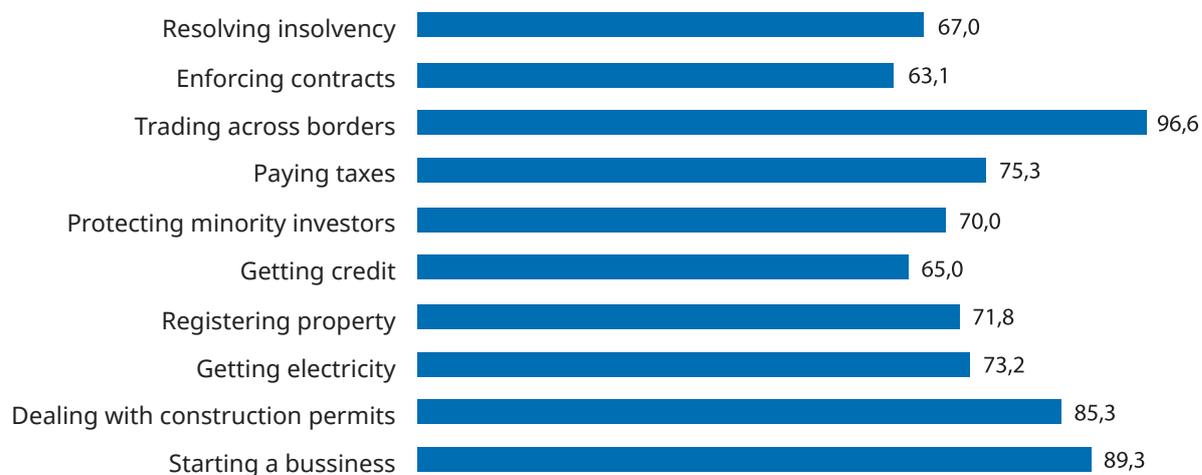
42 Regulatory quality percentile rank indicates the country's rank among all countries covered by the aggregate indicator, with zero corresponding to lowest rank and 100 to highest. In line with this, the regulatory quality percentile rank of Serbia was 60.1 in 2019, compared to Hungary at 72.6, Croatia at 72.12, Slovenia at 80.2 and Austria at 91.35.

43 Indicators consulted for this assessment mostly consider the type of regulatory solution used for a certain operation, instead of real occurrences on the market (such as the number of days to obtain a permit).

44 World Bank (2020), Doing Business: Serbia 2020.

Figure 7. Ease of Doing Business Index


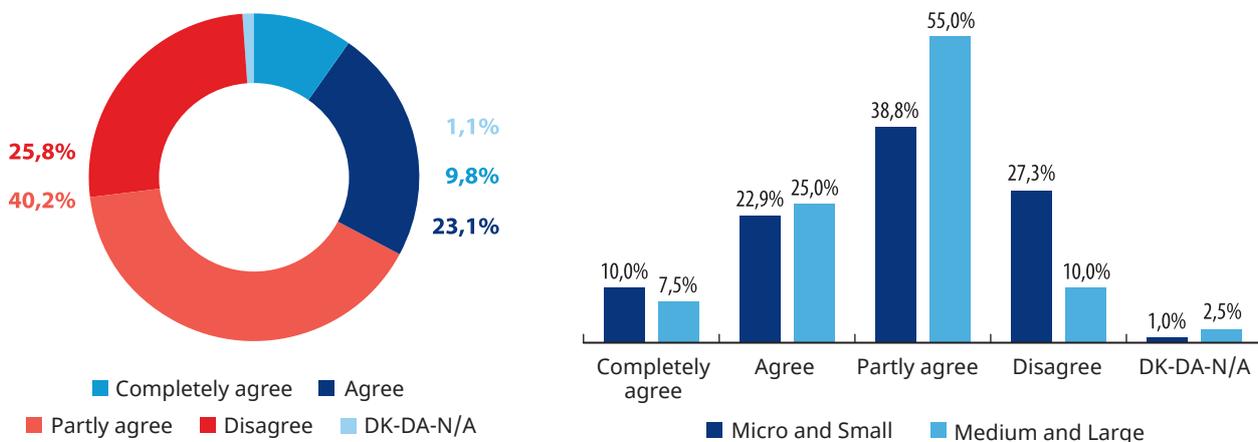
Source: World Bank, Doing Business Project.

Figure 8. Ease of Doing Business in Serbia, 2020


Source: World Bank, Doing Business Project.

Despite recent improvements, enterprises, in particular micro and small ones, encounter difficulties in understanding and following the business regulations. Overall, about one third of respondents (32.9 per cent) agreed that the legal and regulatory framework was easy to understand and follow (Chart 8). A further 40.2 per cent agreed only to some extent with the statement, while a quarter of respondents (25.8 per cent) disagreed completely. Larger enterprises find the legal and regulatory framework easier to understand and follow compared to the smaller ones. Only 10 per cent of respondents from medium-sized and large enterprises noted that the current legal and regulatory framework was difficult to understand and follow compared to 27.3 per cent of those from micro and small ones.

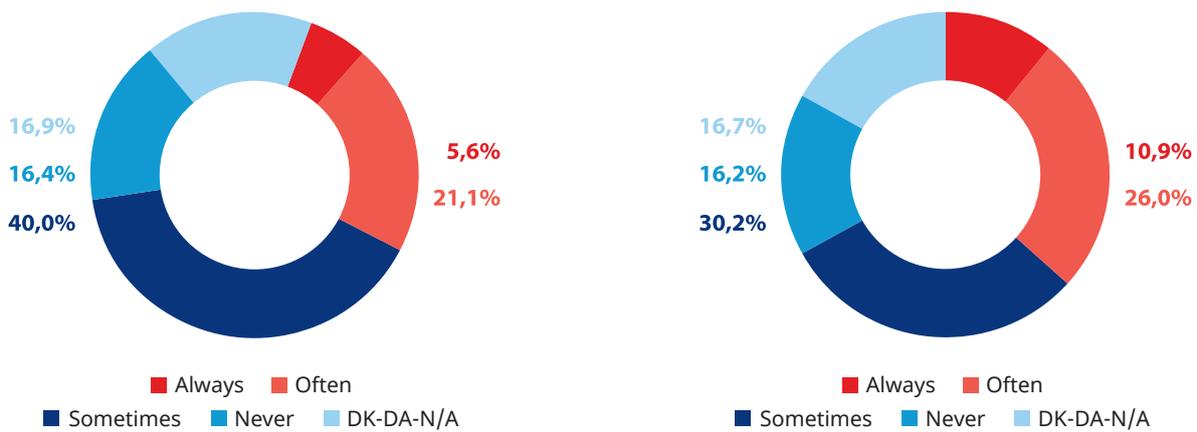
Chart 8. Are laws and business regulations in Serbia easy to understand and follow? All enterprises (left) and enterprises by size (right)



Source: EESE survey.

Enterprises deal frequently with overlapping regulatory bodies, which entails additional business costs. Precisely, the majority of EESE respondents (66.7 per cent) reported that their enterprises deal with overlapping regulatory bodies either on a regular basis (26.7 per cent) or occasionally (40 per cent) (Chart 9). Asked about separate costs paid to each regulatory body, the majority of EESE respondents (67.1 per cent) reported that they had made such payments. In particular, more than a quarter (26.9 per cent) of respondents made payments regularly while near a third (30.3 per cent) did the same in some cases. It should be noted that Serbia has invested significant efforts to digitalize some administrative procedures. Yet, more adjustments are needed between regulations and regulatory bodies to make administrative processes more efficient. Additionally, focus group discussions highlighted that further digitalization would positively impact on businesses. For instance, documenting licences online and organizing a comprehensive online register would relieve enterprises of carrying along unnecessary papers.

Chart 9. Do enterprises have to deal with overlapping regulatory bodies (left) and do they have to pay separate costs to each regulatory body (right)?

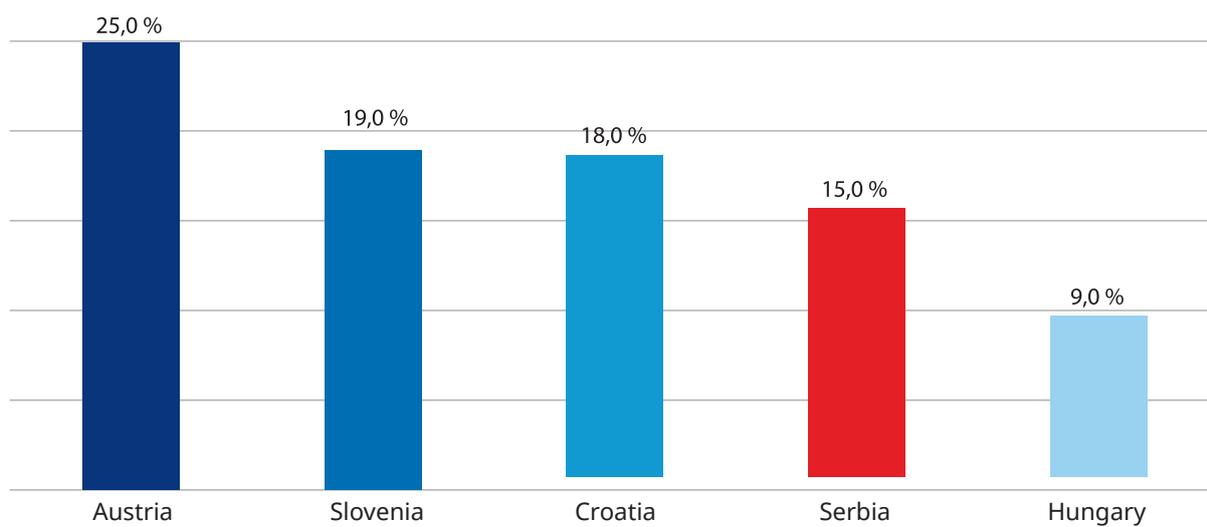


Source: EESE survey.

3.3 Taxation

Tax revenue is the most important income source of the state budget in Serbia, contributing 85.43 per cent of total revenues planned for 2021.⁴⁵ The largest part of tax revenue was expected to be collected through value-added tax (VAT) (44.92 per cent) and excises (23.63 per cent), while corporate taxes amounted to 7.42 per cent and personal income taxes amounted to 5.49 per cent.⁴⁶ In Serbia, corporate income tax is flat at 15 per cent.⁴⁷ In comparison to the reference countries, only Hungary has a lower rate (9 per cent), while Austria has the highest corporate tax rate of 25 per cent (Figure 9).

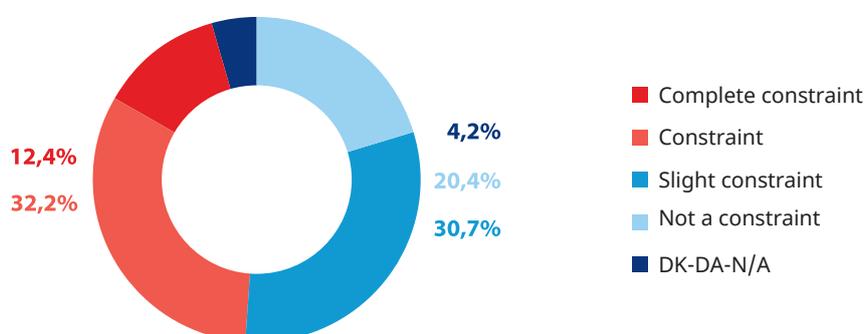
Figure 9. Corporate income tax rates, 2020



Source: Trading Economics.

The EESE respondents were divided when asked whether the size of the tax burden was a major constraint on the investment plan of their enterprises. Thus, almost half of respondents (44.6 per cent) perceived the size of the tax burden as a complete constraint or constraint on the investment plans of their enterprises, while a third of respondents (30.7 per cent) perceived it as a slight constraint (Chart 10). However, around one fifth (20.4 per cent) of respondents did not perceive the size of tax burden as a constraint at all.

Chart 10. Is the size of the tax burden on businesses a major constraint on the investment plans of enterprises?



Source: EESE survey.

⁴⁵ Ministry of Finance of the Republic of Serbia (2021), Citizens' guide through budget of the Republic of Serbia, https://www.mfin.gov.rs//upload/media/sua5Ig_603dfe4bda1ea.pdf

⁴⁶ Ibid.

⁴⁷ See <https://tradingeconomics.com/country-list/corporate-tax-rate?continent=europe>.

An overwhelming majority of EESE respondents perceived taxes as profit insensitive and noted that tax deductions were not available for small businesses. Precisely half of business representatives reported that taxes are profit insensitive, meaning that taxes are paid regardless of whether the company is making profit or not (Chart 11). In addition, more than a half of EESE respondents (52.4 per cent) stated that rebates were not available for loss-making small businesses, which is seen as a major constraint for MSMEs development, as re-enforced during the focus group discussions (Chart 12). Furthermore, 31.2 per cent believed that tax deductions for enterprises making investments in equipment and facilities were not available (Chart 13). Contrary to the perception of most of EESE respondents, the Act on Corporate Income Tax provides for a tax holiday, albeit only for large investors. Large investors, who invest at least 1 billion Serbian dinars (approximately €8.6 million) and employ at least 100 workers for an indefinite time are entitled to a tax holiday of ten years. However, it is unlikely that small business would be able to make such investments. Therefore, the tax deductions are effectively available only for the large firms.

Chart 11. Are taxes “profit-insensitive”?

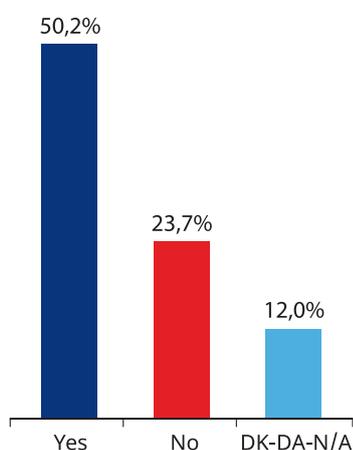


Chart 12. Are tax rebates available for loss-making small businesses?

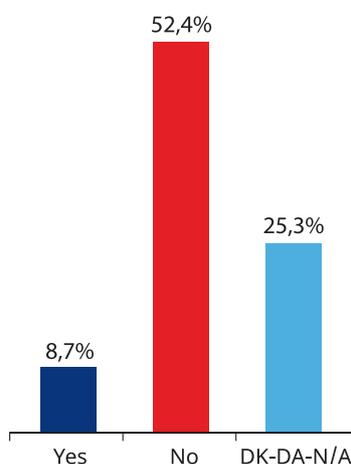
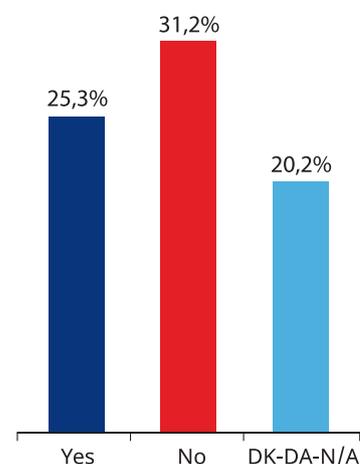


Chart 13. Are tax deductions available for companies to invest in equipment and facilities?



Source: EESE survey.

Despite some improvements made in the legislative area, enterprises in Serbia still face a high level of payments originating from indirect taxation,⁴⁸ with parafiscal charges being the most pressing ones.⁴⁹ The legislation, adopted in December 2018, aimed to reduce the complexity and uncertainty of parafiscal charges by removing or merging some of them. However, the problem has not been addressed enough as some charges were reintroduced at a later stage.⁵⁰ This was confirmed by the preliminary findings of a recent research which identified as many as 1.200 parafiscal charges only at state level based on the analysis of 200 laws and 300 bylaws. In addition, the analysis of the sample of local self-governments showed that the average amount of the tax is RSD 7,500 (EUR 64), while their number ranges from 10 in Ruma to as many as 144 in the municipality of Knjaževac.⁵¹

Tax administration is perceived as a constraint mainly due to the high frequency of payments made in a year, and time requested to deal with tax payments. The World Bank’s Doing Business Project records the taxes and mandatory contributions that a medium-size company must pay or withhold in a given year, as well as the administrative burden of paying taxes and contributions and complying with post filing procedures (VAT refund and

48 European Commission Fact Sheet (2018), Key findings of the 2018 Report on Serbia.

49 SAE (2015), Research about the costs of doing business of SMEs related to the implementation of the regulation in the Republic of Serbia: The profit tax is low but making profit is difficult.

50 European Commission (2020), Serbia 2020 Report.

51 Partner Solutions, NALED, KPMG and Institute Mihajlo Pupin, Analysis of local non-tax levies, 2021 (supported by USAID and presented for the purpose of the campaign “Month of Parafiscal”), <https://naled.rs/en/vest-kroz-upis-u-javni-registar-do-vece-transparentnosti-lokalnih-neporeskih-dazbina-5193>

tax audit). According to the analyses, the total tax and contribution rate as a percentage of profit is lower in Serbia than the average rate for high-income members of the Organisation for Economic Co-operation and Development (OECD), and only slightly higher than the average rate of the Europe and Central Asia (Table 1). However, the number of payments made in a year, as well as time required to comply with taxes are considerably higher than in the comparison regions. This may explain why tax administration is perceived as a constraint.

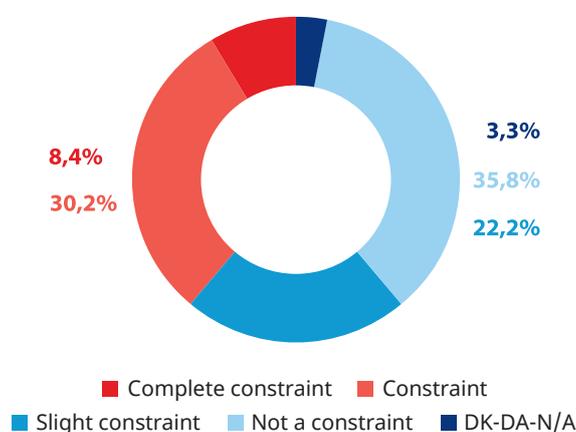
Table 1. Paying taxes, 2020

Indicator	Serbia	Europe and Central Asia	OECD high income	Best regulatory performance
Payments (number per year)	33	14,4	10,3	3
Time (hours per year)	226	213,1	158,8	49
Total tax and contribution rate (percentage of profit)	36,6	31,7	39,9	26,1

Source: World Bank, Doing Business Project.

The views of EESE respondents on the issue of tax administration were divided. Approximately 40 per cent of EESE respondents consider tax administration either a complete constraint or a constraint (to doing business (Chart 14) despite some progress made in legislative alignment with EU rules on taxation. A further 22.2 per cent see it as a slight constraint, while 35.8 per cent of respondents do not perceive it as a constraint at all.

Chart 14. Do enterprises consider tax administration to be a major constraint to doing business?



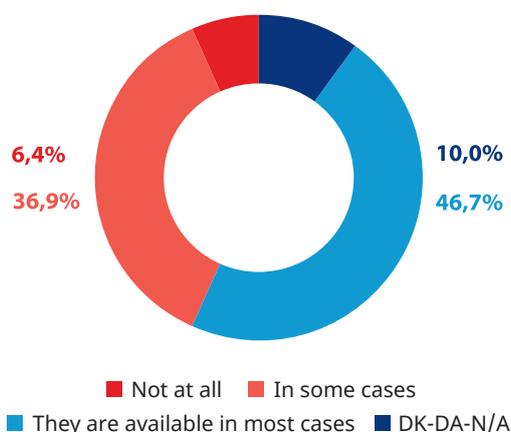
Source: EESE survey.

As a result of digitalization of tax administration, a significant majority of EESE respondents (83.6 per cent) reported that the electronic system for filling documents were available to help enterprises reduce the tax burden (Chart 15). Thus, most of the respondents have used the portal eTaxes and experienced a positive impact on business. The portal is an electronic service of the Serbian Tax Administration, allowing all taxpayers to submit electronically signed tax return forms, monitor status of sent returns and view the balance on their accounts.⁵² While the digitalization process should continue, administrative capacities and adequate staffing need to be further strengthened as well.⁵³

52 Government of the Republic of Serbia (2018), eTaxes, The Future is Now, www.srbija.gov.rs/tekst/en/129961/etaxes.php.

53 European Commission (2020), Serbia 2020 Report.

Chart 15. Are electronic filing and payment systems available to help enterprises reduce the tax burden while easing the administrative requirements?

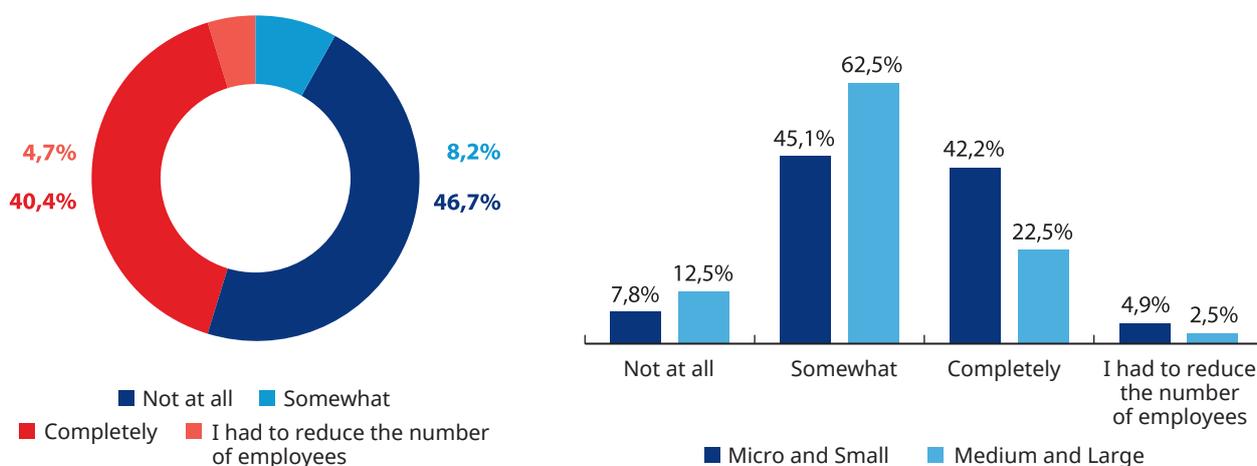


Source: EESE survey.

3.4 Labour taxation

Almost half of EESE respondents perceive labour costs as a barrier to increasing the number of employees in their companies. Micro and small enterprises are more affected with 42.2 per cent reporting a negative impact compared to 22.5 per cent of representatives from medium-sized and large enterprises (Chart 16). In addition, some 5 per cent of micro and small enterprises had to resort to layoffs as a result of the financial pressure from labour costs compared to 2.5 per cent of medium-sized and large enterprises. An overwhelming 95 per cent of participants in focus group discussions rated labour costs as having a major negative impact on their businesses. According to the legislation in force, companies are obliged to make social security contributions on an employee's salary, namely pension and disability insurance at the rate of 14 per cent, health insurance 5.15 per cent, and unemployment insurance 0.75 per cent.

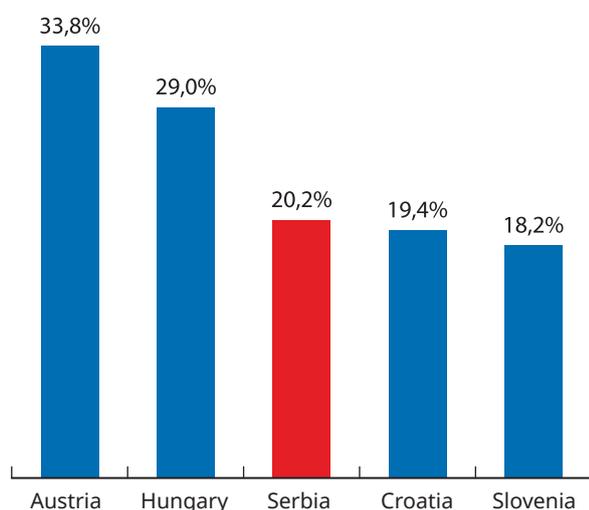
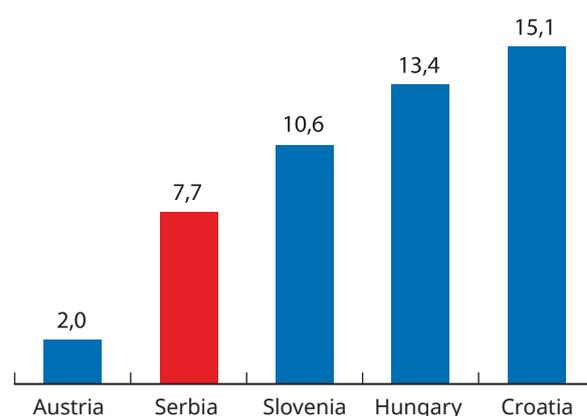
Chart 16. Do taxes paid on wages influence the number of employees? All enterprises (left) and enterprises by size (right)



Source: EESE survey.

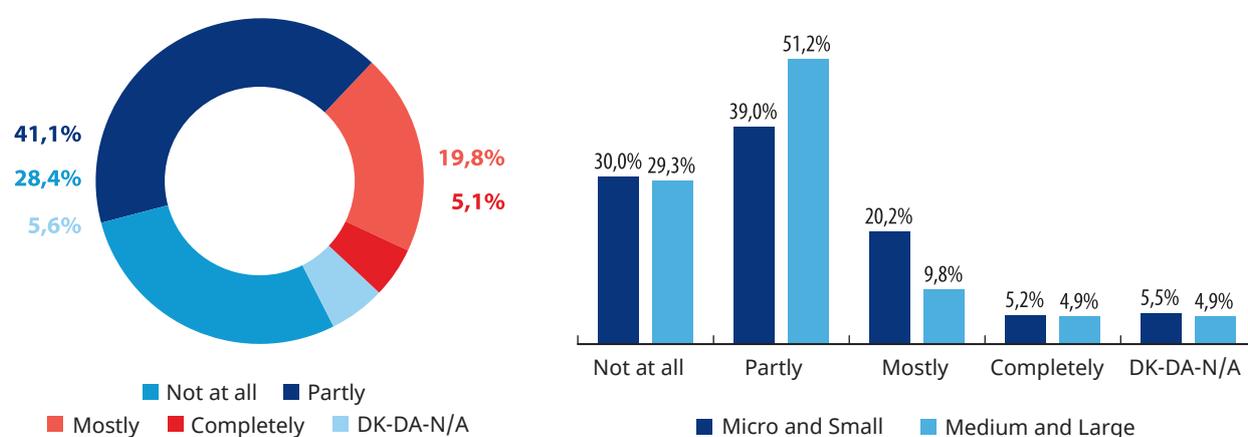
However, compared to the reference countries, the labour tax rate in Serbia is not very high. Thus, the amount of labour taxes and social contributions paid by employers as a percentage of profit is lower in Serbia, amounting

to 20.2 per cent, compared to Austria and Hungary, where these costs for companies are 33.8 per cent and 29.0 per cent of profits, respectively (Figure 10). Moreover, redundancy labour costs measured in weeks of salary are lower in Serbia than in most reference countries (Figure 11). Namely, these costs amount 7.7 weeks of salary in Serbia, while they are 15.1 in Croatia, 13.4 in Hungary and 10.6 in Slovenia. Only Austria has lower redundancy costs at two weeks of salary.

Figure 10. Labour tax rate

Figure 11. Redundancy costs in weeks of salary


Source: World Economic Forum, Global Competitiveness Report 2019.

The wage rates are not aligned with productivity growth dynamics in Serbia. The most important factor for determining the level of wages in a country is the level of productivity in terms of the value of production per worker. Since 2015, the level of wages in Serbia has had a more rapid growth than the level of productivity.⁵⁴ A quarter of EESE respondents noted that wages were completely out of sync with productivity, while 41.1 per cent reported that they only partly exceeded productivity growth (Chart 17). The share of micro and small enterprises (25.4 per cent) reporting that wage growth exceeded productivity growth completely was relatively higher compared to the share of medium-sized and large enterprises (14.7 per cent) sharing the same perception.

Chart 17. Have increases in wages and related labour costs exceeded productivity growth at the enterprise level? All enterprises (left) and enterprises by size (right)


Source: EESE survey.

54 World Bank Group (2020), Serbia Systematic Country Diagnostic Update.

4. Fair competition

4.1 Overview of legislative, policy and institutional framework

The Serbian legislative framework in the area of competition is in line with the EU acquis but the actual implementation needs to be further strengthened. The first law on protection of competition was adopted in 2005. The law established a system of merger control and committed to ensuring equal treatment of private and public undertakings. Furthermore, the Commission for Protection of Competition (CPC) was set up in 2006 as the main institution responsible for the implementation and enforcement of the new law. Despite bringing about numerous legal and institutional changes, the law had serious procedural limitations. Among other things, the CPC did not have power to impose sanctions on undertakings.⁵⁵ Moreover, as the thresholds for merger notification had been set at a low level, the CPC was overloaded with abundant requests for authorization, which absorbed more than 80 per cent of its working capacity, limiting its resources for investigating cartels and abuses of dominance. To address shortcomings of the first law, a new law on protection of competition entered into force in 2009 (followed by the adoption of several by-laws and its subsequent amendment in 2013), which brought the legislative framework in line with the Treaty on the Functioning of the European Union and international standards. The current law on protection of competition provides for an ex-ante control of mergers. However, the legislative framework has yet to be fully brought into line with EU guidelines in this area.⁵⁶ Work on a new law on protection of competition aiming at further alignment with the EU acquis has halted.

The Commission for Protection of Competition is the main authority responsible for implementing the competition legislation. The institution is operationally independent, but more efforts are needed to make competition enforcement more impactful. The CPC is accountable for its work before the National Assembly, to which it must submit annual reports. The CPC has powers to investigate, sanction and remedy anti-trust infringements, such as restrictive horizontal and vertical arrangements and exclusionary or exploitative practices by dominant companies. In addition, the CPC has wide advocacy competencies. It supervises competition conditions in specific markets or sectors, issues opinions on draft or existing regulations that affect competition, and cooperates with relevant state institutions to improve the implementation of competition rules. The CPC needs to improve its enforcement records. In 2020 the CPC adopted six decisions on restrictive agreements and one on abuse of dominant position. A total of 18 raids were conducted, while its leniency programme was not used.⁵⁷ The level of imposed fines of approximately €535 million increased compared to 2019 (€0.86 million) but it was yet substantially lower than in 2018 (more than €3.8 billion).⁵⁸ In the area of advocacy, it issued five opinions on draft legislation (although not all were considered) and launched seven sector enquiries. To improve its performance, CPC needs to further strengthen its institutional capacity and grow the number of staff. Currently, the CPC has 56 employees of which 30 are case handlers with adequate expertise.⁵⁹ In addition, competition enforcement is seriously hampered by limited institutional capacity and specialization of the judiciary to deal with complex competition cases. The number of CPC decisions upheld by appeal courts continued to increase in 2020.⁶⁰

Fair competition is negatively affected by the large informal economy. The informal economy has been slowly shrinking over the years, but the share of informal employment remains high. In 2020, the share of informal employment, two thirds of which was in agriculture, fell to 16.4 per cent of total employment from 18.3 per cent in 2019.⁶¹ Driving forces behind the informal economy include excessive taxation, over-regulation and weak en-

55 UNCTAD (2011), Voluntary Peer Review of Competition Law and Policy: Serbia, Full Report.

56 European Commission (2021), Serbia 2021 Report.

57 Ibid. It should be noted that the leniency programme was used in a bid-rigging case in 2019, for the first time since its introduction in 2015.

58 Ibid.

59 The total number of CPC staff has been steadily growing over the past few years, from 39 in 2015 to 52 in 2019 and 56 in 2020. This figure is limited but reasonable compared with OECD and non-OECD countries. In comparison, according to OECD data, the 15 competition authorities in small economies (with a population below 7.5 million) had an average of 114 staff in 2019, of whom 43 were working on competition.

60 European Commission (2021), Serbia 2021 Report.

61 SORS, www.stat.gov.rs/en-us/oblasti/trziste-rada/anketa-o-radnoj-snazi/.

forcement capacity. Due to an accelerated economic growth in the pre-crisis period, there was an increase in the share of formalized employment. The COVID-19 crisis highlighted the fragility of informal employment. The rate of informal employment decreased by 1.8 per cent, with most jobs lost in the informal sector. Notable efforts have been made to tackle the informal sector, but the pace of reform implementation is slow.⁶² With the adoption of the law on inspection control in 2015, the outdated and contradictory regulations⁶³ of the old system were eliminated and the inspection coordination was significantly strengthened. In addition, in 2019, the Government adopted an action plan for the implementation of the National Programme for Countering the Shadow Economy for 2019–2021, which aims at further improvement of the work of inspection bodies, a tougher penalty policy and more efficient tax collection. A new law⁶⁴ that entered into force in 2019 has simplified the employment of seasonal workers in certain activities, among which agriculture, through a new type of contract that allows for easier registration.

The continuing large presence and preferential treatment of state-owned enterprises hampers competition in Serbia. While the State continues to withdraw from direct involvement in the economy in general, its presence remains strong. State-owned enterprises continue to dominate many sectors of the economy, including energy, transportation, utilities, telecommunications, infrastructure, mining and natural resource extraction. This outsized presence of state-owned enterprises deters private investment and innovation, impedes overall competitiveness and poses substantial fiscal risks.⁶⁵ State-owned enterprises dampen productivity with their own inefficiencies, and when they are shielded from full competition, private companies face greater hurdles to offer alternatives.⁶⁶ Many state-owned enterprises operate with low efficiency and high costs, also due to higher wage bills. Governance of state-owned enterprises also continues to pose problems by irregular appointments of acting managers for extended periods instead of using the standard nomination process.⁶⁷ Public companies account for 19 per cent of value-added and formal employment, but they receive 60 per cent of corporate subsidies.⁶⁸ Foreign investors also benefit from preferential treatment compared to domestic businesses. For instance, according to some estimations out of €5 spent on subsidies, €4 go to foreign enterprises⁶⁹ as the high entry criteria fixed costs (for example, required audit reports by the Big Four⁷⁰) make state aid inaccessible to small domestic enterprises.

4.2 Competition intensity

Despite improvements in the legislative area, competition in the Serbian market is not very intense. The intensity of local competition indicates the degree to which competitors in a given market are perceived to pressure on one another (in terms of lowering prices, improving the quality of products and services) while struggling for market share and profit. It depends on various factors such as the degree of concentration of competitors in an industry, market growth rate, differentiation of products and services, and level of intellectual property protection, among other things. In 2017 Serbia ranked 115 out of 137 economies on the intensity of local competition index, indicating that the Serbian market was rather concentrated. On a more positive note, despite continuously falling behind reference countries between 2013 and 2017 (except for Hungary in 2017), Serbia has been gradually making some evident progress (Figure 12). Among reference countries, it had the highest year-on-year average index growth rate of 4.2 per cent from 2013 to 2017.

62 European Commission (2021), Serbia 2021 Report.

63 Prior to the adoption of the law, there were many different regulations unified regulations on inspection, which were at times contradictory. For instance, inspectors were not able to exercise oversight over unregistered economic activity.

64 Law on simplified employment in seasonal jobs in certain activities, 2018, Official Gazette of RS No. 50/18.

65 European Commission (2021), ERP of Serbia 2021–2023.

66 World Bank (2020), Serbia Updated Systematic Country Diagnostic Report.

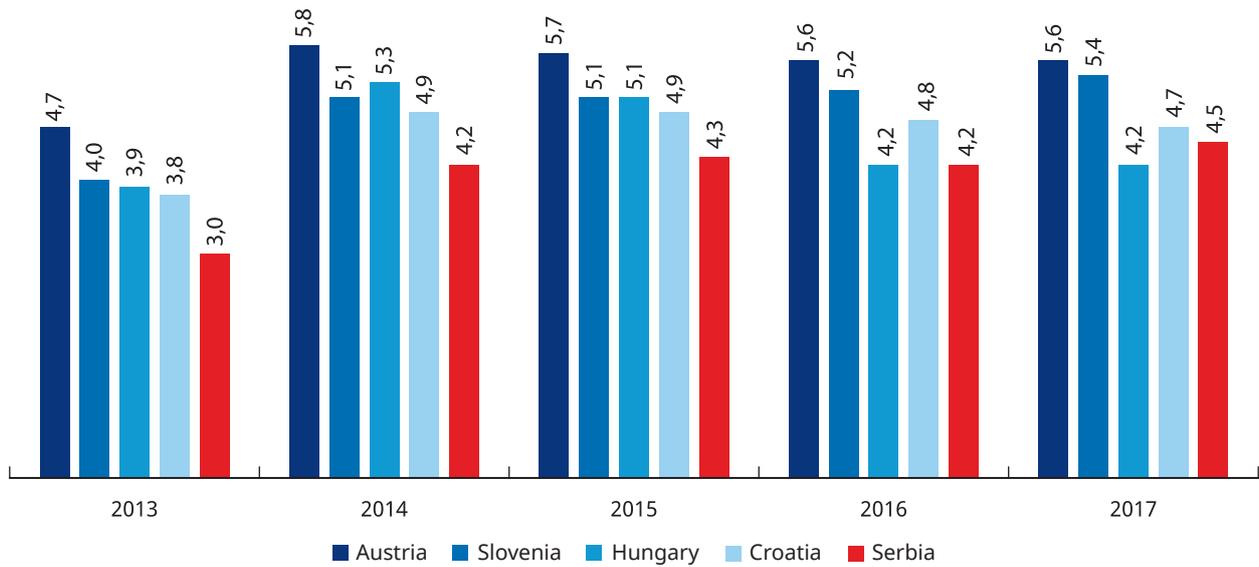
67 According to Transparency Serbia, only 9 out of 34 public companies have legally elected directors, while 22 are led by acting managers, 19 of which have expired mandates, since the law on public enterprises limits that status to 12 months.

68 European Commission (2021), ERP of Serbia 2021–2023.

69 CEVES estimations.

70 The Big Four refers to Deloitte, Ernst & Young, KPMG and PwC.

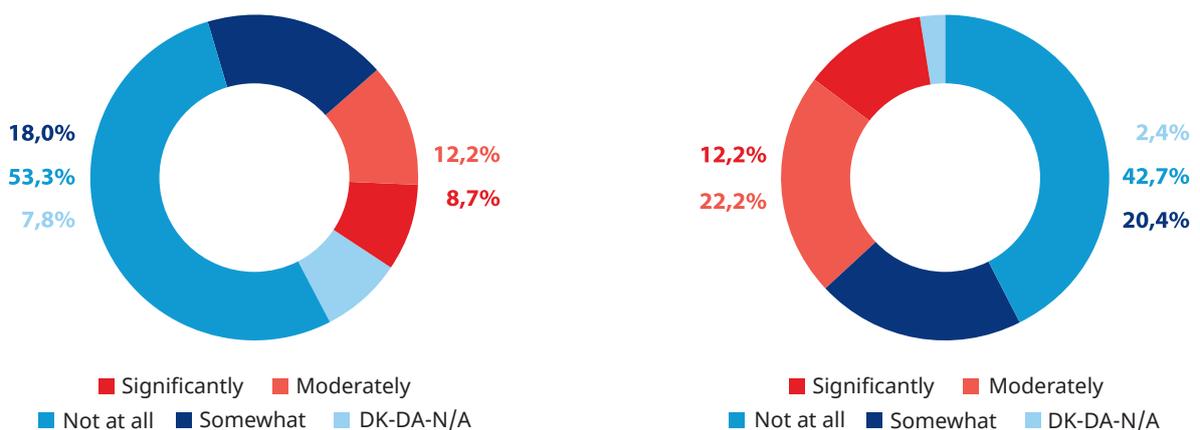
Figure 12. Intensity of Local Competition



Source: World Economic Forum Executive Opinion Survey.
 Note: 1 = not intense at all to 7 = extremely intense. The Global Competitiveness Report discontinued issuing its index on intensity of local competition since 2018.

The scarce competition intensity in Serbia has been confirmed by the EESE survey results. Only 8.7 per cent of respondents reported very significant price reductions in response to domestic competition, a further 30.2 per cent reduced prices moderately or insignificantly, while the majority (53.3 per cent) made no price reductions at all (Chart 18). When it comes to foreign competition, a slightly higher share of respondents reported having reduced prices significantly (12.2 per cent), 42.6 per cent reported moderate or insignificant price cuts and 42.7 per cent noted that they did not make any price adjustments in response to foreign competition.

Chart 18. Has your company significantly reduced the price of its main product in response to price reductions by domestic (left) or foreign (right) competitors?

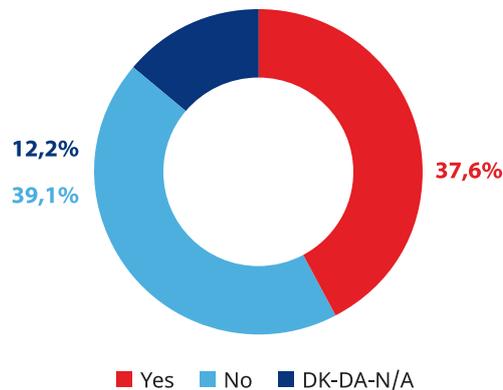


Source: EESE survey.

4.3 Monopolistic practices and the effectiveness of anti-trust legislation

With pronounced differences across the sectors, the opinions of EESE respondents were divided when asked about the existence of monopolies and monopolistic practices in Serbia. While 37.6 per cent of respondents were convinced that monopolies or monopolistic practices existed in their sector, an almost equal share (39.1 per cent) indicated the opposite (Chart 19). Although monopolies/monopolistic practices are perceivably present in many sectors, focus groups participants indicated that other forms of anti-competitive behaviour pose an even greater threat to fair competition. In particular, the competition from enterprises operating in the informal sector was perceived as a major threat followed by the privileged foreign investors and state-owned enterprises.

Chart 19. Do monopolies or monopolistic practices exist in your sector?

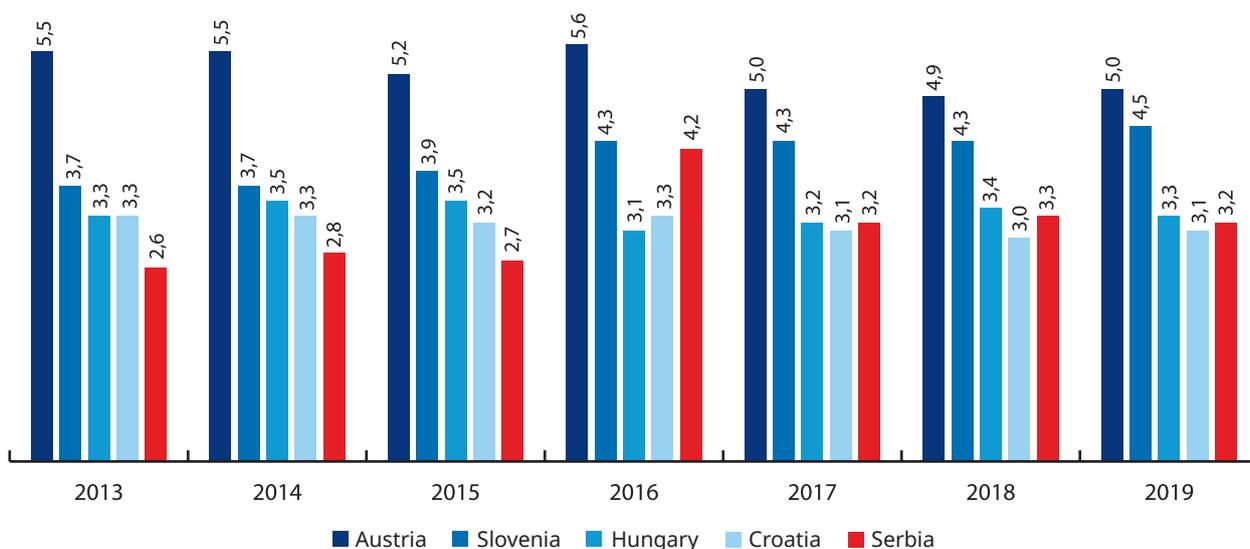


Source: EESE survey.

Although Serbia experienced a slow but steady improvement in the area of competition, monopolistic practices remain present, which explains the divergence of opinions of EESE respondents. In 2019, Serbia ranked 110 out of 141 countries on market dominance. The extent of market dominance is measured by rating the corporate activity from 1 (corporate activity is dominated by a few business groups) to 7 (activity is spread among many companies). In 2019 the index value for Serbia was 3.2 and it was much lower than in Austria (5.0) or Slovenia (4.5), and only slightly higher than in neighbouring Croatia (3.1) (Figure 13). Although the state of competition was improving between 2013 and 2019, all comparator countries fared (at least) slightly better – while the average value for Serbia over the seven-year period was 3.2, while Austria, which had the best performance, had an average of 5.4.

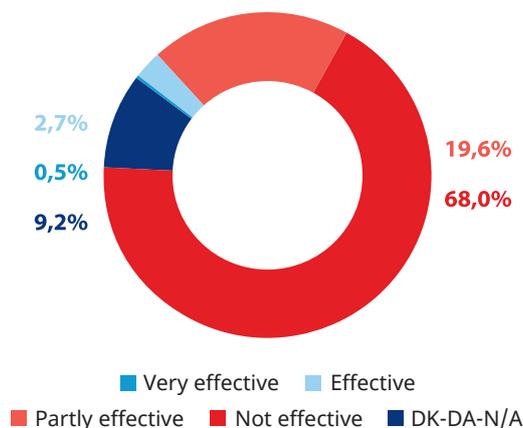
Anti-monopoly policies are perceived as rather ineffective by enterprises in Serbia. The majority of EESE respondents (68 per cent) expressed the opinion that anti-trust legislation was ineffective with a further 19.6 per cent assessing it as partly effective (Chart 20). Only an insignificant share of respondents (3.2 per cent) believed that anti-trust legislation was effective or very effective. Focus group discussions revealed that enterprises believed there was no true commitment from the Government to enforce fair competition. An interesting illustration is that 80 per cent of enterprises (that participated in focus groups) never filed a complaint against unfair competitors, some because they were unsure which authority to contact. Out of those that did, only 10 per cent received a response and were ultimately satisfied with the process. In fact, the majority of respondents (70 per cent) never received a response to their complaint.

Figure 13. Market Dominance Index



Source: World Economic Forum Executive Opinion Survey.

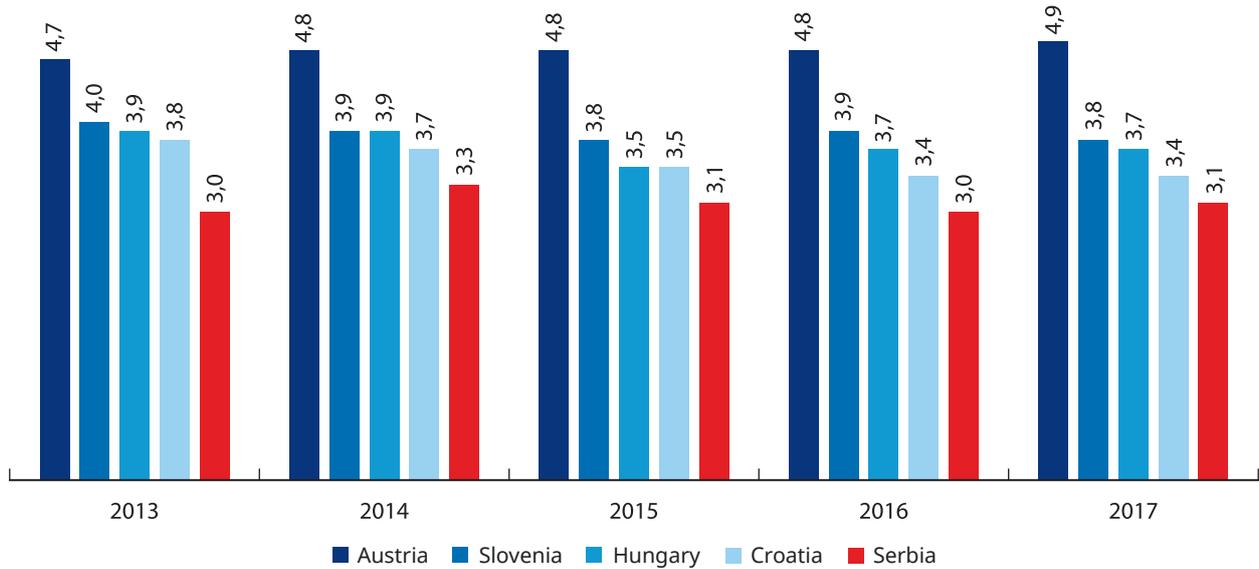
Chart 20. How effective is anti-trust legislation?



Source: EESE survey.

The ineffectiveness of anti-monopoly polices in Serbia has been further confirmed by its position in international rankings. Effectiveness of anti-monopoly policy index, based on annual survey data, can range from 1 (policies are not effective at promoting competition) to 7 (policies are effective at promoting competition). In 2017, with the index value of 3.1, Serbia ranked 114 out of 137 countries. The same value (3.1) was its average throughout the reference period (2013–2017), increasing only minimally over the years (Figure 14). This means that not only was anti-monopoly policy in Serbia perceived as much less effective compared to other reference countries, but there was also almost no progress in the reference period.

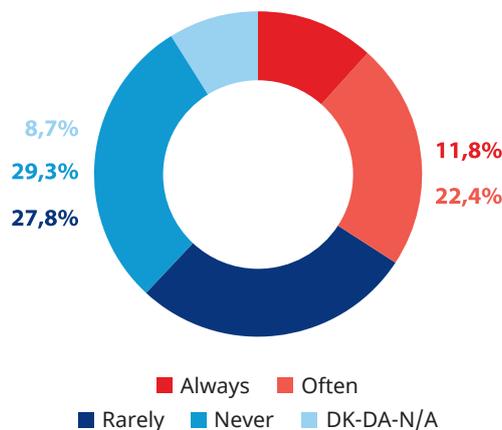
Figure 14. Effectiveness of anti-monopoly policies



Source: Source: World Economic Forum Executive Opinion Survey.
 Note: Respondents to the World Economic Forum Executive Opinion Survey rate the extent to which anti-monopoly policy promotes competition in their country from 1 (does not promote competition) to 7 (effectively promotes competition). The Global Competitiveness Report discontinued issuing its index on effectiveness of anti-monopoly policies since 2018.

The widespread informal sector hampers fair competition in Serbia. More than a third (34.2 per cent) of EESE respondents reported that they always or often competed against unregistered or informal businesses. A further 27.8 per cent noted that they rarely competed with informal companies and 29.3 per cent never faced competition from the informal sector (Chart 21). To combat informal employment, the authorities have established a working group chaired by the labour inspectorate. Another tool is a single information system for inspections (e-Inspector), which aims to ensure better coordination among various inspections. A special working group for coordination of inspection activities related to the COVID-19 pandemic was established in October 2020.

Chart 21. Does your enterprise compete against unregistered or informal businesses?



Source: EESE survey.

5. Access to finance

5.1 Overview of legislative, policy and institutional framework

Enabling enterprises to access finance is one of the strategic priorities for the development of the MSME sector.

The Strategy for supporting the development of SMEs, entrepreneurship and competitiveness for the period 2015–2020 focuses on improving access to sources of funding, with particular attention to improving the quality of services and the offer of the banking sector to SMEs, developing new financial instruments, and improving the ability of SMEs to access various sources of financing. The Serbian Ministry of Economy is in joint charge of monitoring the implementation of the SME Strategy with the Council for SMEs, Entrepreneurship and Competitiveness, which became operational in November 2017, two years after it had been formally established. In addition to monitoring and coordinating the implementation of the SME Strategy, it also provides suggestions and initiates customized programmes for SMEs.

The financial sector of Serbia is bank dominated. Bank lending remains the main source of private sector financing, at 43 per cent of GDP in 2017.⁷¹ The banking sector accounts for around 92 per cent of the assets of the overall financial sector, which is considerably more than in the EU (70 per cent). As of end 2020, there were 26 banks operating in the economy. This is a relatively large number compared to similar economies (for example, there are 13 banks operating in Hungary, 16 in the Czech Republic and 17 in Bulgaria).⁷² Overall, the banking sector in Serbia is relatively well-developed and competitive.⁷³ In 2018, the number of bank loans to SMEs increased by 17.2 per cent year-on-year, alongside the share of new SME loans in total corporate loans – 44.5 per cent in 2018.⁷⁴ SME lending has accelerated due to decreasing interest rates and the banking system's overall liquidity.⁷⁵ Precisely, interest rates for SME loans in or indexed to foreign currencies decreased to 4.2 per cent in 2018 (from 4.6 per cent in 2017 and 5.7 per cent in 2016).⁷⁶

The institutional infrastructure in charge of providing financial services and supporting MSME financing is relatively solid. It includes mainly commercial banks and a smaller range of microfinance institutions, leasing companies, factoring companies, and private equity and venture capital companies. There are also several government programmes supporting MSME financing. Two institutions are in place to support the implementation of national credit guarantee schemes. Precisely, the Serbian Development Fund was established in 1992 to issue guarantees to commercial banks' lending at subsidized interest rates to SMEs. Similarly, the Serbian Export and Insurance Agency, set up in 2005, issues guarantees and other forms of sureties for export businesses and investments abroad. The Innovation Fund is another government institution, established in 2011, specialized in providing financial support to young high-growth companies mainly in the technology sector. The Development Agency of Serbia, established in 2016, provides business support services to both domestic and foreign companies. In particular, it supports direct investments and export promotion, as well as projects that enhance the attractiveness of Serbia to foreign investors.

Government support programmes need to diversify their offer and the eligibility criteria for MSMEs, while institutions responsible for the implementation of these programmes need to improve their corporate governance, operational efficiency and accountability. An independent evaluation completed in 2017 revealed significant challenges and weaknesses in the activity of the Development Fund and Serbian Export and Insurance Agency, namely the lack of proper oversight and governance, poor credit policies and decisions as well as limited accountability, among other things.⁷⁷ Consequently, the Government adopted conclusions on both institutions, mandating

71 OECD (2019), SME Policy Index: Western Balkans and Turkey.

72 OECD (2021), Competitiveness in South East Europe: A policy outlook.

73 Ibid.

74 National Bank of Serbia (2019), Annual survey on SMEs 2018.

75 In light of the COVID-19 pandemic, efforts were made (through national guarantee schemes) to further facilitate MSME access to commercial bank loans. Indeed, according to the latest report on bank credit activity (for Q1 2021), while some requirements (in terms of collateral or maximum loan amount) have been recently made stricter due to increased aversion towards risk, others have been slightly loosened for MSMEs – a result of monetary policy loosening and more favorable financing conditions for this market segment.

76 National Bank of Serbia (2019), Annual survey on SMEs 2018.

them to address the challenges and identify options for more effective provision of development finance for the business sector. A recent review of government support programmes found that few are supporting start-ups or early-stage high-risk businesses (apart from those offered by the Innovation Fund).⁷⁸ It was also recommended that programmes should be better targeted at MSMEs with good growth potential rather than those generally eligible.

5.2 Alternative sources of finance

Alternatives to bank financing have remained either limited or not yet sufficiently regulated to ensure the uptake of non-bank financial instruments. Access to a sufficiently broad range of financing instruments is crucial for obtaining the type and volume of financing that best suits the specific needs of MSMEs at every stage of the enterprise life cycle. Alternative sources of finance are particularly valuable for and used by microenterprises, entrepreneurs and start-ups that would hardly otherwise access traditional financing sources. Alternatives to bank financing have increased lately. However, not all of them are regulated yet, while those that are remain underdeveloped, despite some recent positive developments. A description of the current non-bank financial instruments available and their level of development is provided below.

The factoring market is still in an early stage of development despite Serbia having had a dedicated law on factoring since 2013.⁷⁹ Factoring⁸⁰ is mainly driven by banks. As of December 2018, there were 18 factoring providers including one state-owned provider (the Serbian Export Credit Agency). Factoring products offered are reflective of a market in its early stages of development.⁸¹ The law on factoring was amended in 2018 (following an EBRD assessment) introducing new requirements for end-borrowers. However, further clarification is required to define local providers' obligations to perform due diligence on customers, and the Serbian Government is yet to take comprehensive action in response to the recommendations.⁸²

The financial leasing market in Serbia is relatively small, but it has been growing since 2016⁸³, after being hit hard by the financial and economic crisis in 2008. Financial leasing companies⁸⁴ are regulated and supervised by the National Bank of Serbia. As of June 2020, 17 financial leasing companies were operating in Serbia. So far, financial leasing was primarily provided for freight vehicles, minibuses and buses and passenger cars.⁸⁵ The law on financial leasing of 2003 was amended in 2011 to regulate financial leasing activities. In December 2020, new amendments were adopted allowing financial leasing companies to be engaged in operating leasing. As of January 2021, the Financial Leasing Register, which centralizes contracts of financial lease of movable and immovable assets, started to allow all types of registration applications to be submitted in electronic form, removing thus some of the administrative burden on enterprises.⁸⁶

The market for private equity and venture capital is at an early stage of development.⁸⁷ The law on alternative investment funds and by-laws enacted by the Securities Commission became effective in May 2020. The legislative

77 World Bank (2019), Serbia New Growth Agenda: Financing for Growth.

78 World Bank, Public Expenditure Review of Small and Medium Enterprise and Competitiveness Programs in Serbia (draft).

79 World Bank (2019), Serbia New Growth Agenda: Financing for Growth.

80 Factoring is a financial transaction and a type of debtor finance in which a business sells its accounts receivable (such as invoices) to a third party (called a factor) at a discount. A business will sometimes factor its receivable assets to meet its present and immediate cash needs.

81 World bank (2019), Serbia New Growth Agenda: Financing for Growth.

82 OECD (2019), SMEs Policy Index: Western Balkans and Turkey.

83 OECD (2021), Competitiveness in South East Europe: A policy outlook.

84 Leasing is a form of financing assets, in which a leasing company (the lessor) buys the asset for the user (lessee) and rents it to them for an agreed period. In return, the leasing company receives predetermined payments from the user and becomes the legal owner of the asset for the duration of the lease agreement, after which legal ownership is transfer to the user.

85 OECD (2021), Competitiveness in South East Europe: A policy outlook.

86 Ibid.

87 Private equity investment funds are pools of capital from different investors that are managed and invested in private companies in exchange for equity or ownership stake. Private funds usually invest in both mature enterprises and start-ups that present good investment opportunities. Venture capital is a form of private equity financing that primarily invests in small companies with exceptional growth potential and start-ups that are developing new technologies or processes. Venture capital generally comes from well-off investors, investment banks, and other financial institutions.

framework provides detailed regulations governing the manner of investment and the instruments in which private equity and venture capital alternative investment funds may invest; the restrictions, types, and timeframes for subscriptions by members or shareholders; the type and extent of restrictions on investment; the calculation of subscriptions; and the determination of the relevant costs. While no activity has been recorded, Serbian firms are more actively using the Enterprise Innovation Fund, which is an active fund managed by South Central Ventures, StartLabs and Eleven Ventures, focusing on early stage high-growth companies mainly in the technology sector.⁸⁸

The introduction of cryptocurrencies⁸⁹ represent a recent innovation in the area of digital financial products.

The first regulation of cryptocurrencies was adopted in March 2019. This qualified cryptocurrencies as one of the instruments included under the Capital Markets Act. The use of cryptocurrencies is also governed by the law on the prevention of money laundering and the financing of terrorism, amended in 2019. This regulates the services of purchasing, selling or transferring virtual currencies or exchanging such currencies for money or other property through Internet platforms, devices in physical form or otherwise, and custody wallet service providers. In December 2020 the Government adopted the law on digital assets which took effect on 29 June 2021, and which offers a comprehensive framework for the development of digital assets.⁹⁰ However, its effect is yet to be seen.

Microfinancing is poorly represented.⁹¹ A functional microcredit industry may be able to give an opportunity to those in need to become financially self-sufficient. In Serbia, microfinance could help cover the needs of enterprises often ineligible for traditional loans, such as microenterprises, entrepreneurs or start-ups. However, without a clear legal and regulatory framework, it is unlikely though that a sustainable microcredit industry will develop. There are only a few microfinancing organizations which can provide some funding: “Agroinvest” – an affiliate of VisionFund International, Micro Development and MicroFinS. However, they can transfer funds only via commercial banks, which makes the procedure more complex and these assets more expensive to end users,⁹² with yearly interest rates of above 25 per cent.

Similarly, other non-bank finance instruments such as business angels⁹³ and crowdfundings⁹⁴ are emerging.

Although there is no legal framework in place regulating business angels, one network is operating – the Association of Business Angels of Serbia – which is a not-for-profit association of private investors connecting start-ups with investors. With regard to crowdfunding, there are currently neither activities nor any regulation in place. However, the National Bank of Serbia is in the process of drafting a law, which will regulate the conditions and manner of providing group financial services but there is no a clear timeline for this.

5.3 Capital markets

Capital markets in Serbia remain underdeveloped with limited stock-market activity, nascent domestic bond market volumes, and a very small corporate bond market. The only market segment that functions comparatively well is the government bond market. The private sector is not making use of the stock market for its financing needs. The lack of initial public offerings (IPOs) remains the biggest challenge for the Belgrade Stock Exchange and Serbian capital market. The Government never used them as a privatization model for state-owned enterprises, while companies from the private sector are very hesitant to raise capital through IPOs as there are no previous success stories.⁹⁵ In addition, there are no clear procedures, nor any prior experience or specific incentives that would encourage IPOs. It can be assumed that this is a consequence of the financial crisis of 2008. For example,

88 OECD (2021), *Competitiveness in South East Europe: A policy outlook*.

89 A cryptocurrency is a digital currency that represents a form of digital asset. It can be used to buy different goods and services and it uses blockchain technology to ensure integrity of transactional data. Blockchain start-ups are numerous in Serbia, as it is among the top economies for blockchain developers.

90 OECD (2021), *Competitiveness in South East Europe: A policy outlook*.

91 Microfinancing is a type of banking service provided by microfinancing organizations that allows individuals and small businesses that otherwise would have no access to financial services to take on reasonable micro loans safely, and access additional services.

94 Strategy for the Development of Entrepreneurship and Competitiveness, 2015–2020, Ministry of Economy of the Republic of Serbia, 2015.

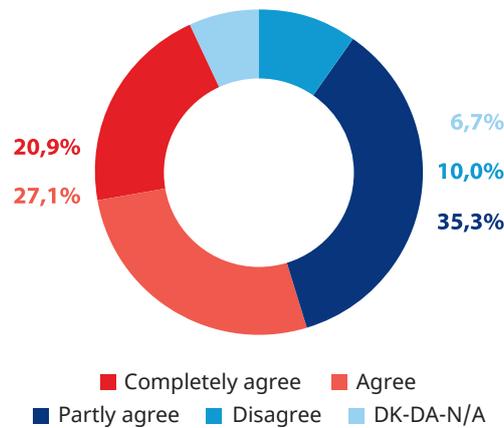
95 Business angels (or angel investors) are independent private investors who invest their own money in new companies with the aim to help entrepreneurs succeed with their innovative business idea. Angel investors are not providing just financial capital but also intellectual one (such as mentoring, know-how).

the daily turnover of securities of the Belgrade stock exchange (BELEX) before the financial crisis was €10 million on average which has declined to €250,000 by 2019. Furthermore, the number of listed companies peaked in 2007 at more than 2,500, but around 75 per cent of companies were ultimately delisted, either voluntarily or through bankruptcy. This only illustrates the currently limited potential of the Serbian equity market. As of January 2020, no new businesses were listed in the “Smart Listing”⁹⁶ segment of the BELEX. On a more positive note, certain initiatives were put in place to revive the BELEX, such as IPO Go! (2018) – a project aiming to increase the supply of investment alternatives and securities.

5.4 Availability of sources of finance

The EESE survey reveals that availability and access to finance is a major developmental obstacle for Serbian enterprises. Almost half of the EESE survey respondents (48 per cent) found access to finance as a major constraint for the establishment and growth of enterprises in Serbia, and 35.3 per cent partially agreed with the statement (Chart 22). This is also supported by the findings of a recent business survey conducted in October 2020, according to which 40 per cent out of 1,100 surveyed enterprises found access to finance as the most significant limiting factor influencing their development and viability, especially in the context of the COVID-19 crisis.⁹⁷ The 2019 World Bank enterprise survey⁹⁸ further reinforces the EESE survey results with access to finance ranking as one of the most frequently cited business obstacles. Furthermore, there is a substantial gap between the enterprise financing needs and actual sources available, especially when it comes to MSME financing. Precisely, the financial gap in Serbia amounted to 28 per cent of GDP in 2017, which was more substantial relative to other Western Balkan countries.⁹⁹

Chart 22. To what extent do you agree with the statement: “Access to finance is a major constraint to the establishment and growth of enterprises in Serbia”?



Source: EESE survey.

Indeed, the lending environment for micro and small enterprises as well as start-ups is still relatively unfavourable. Banking loan services dominate while opportunities for non-collateral-based funding remain very limited.¹⁰⁰ There are no thresholds for loans below which collateral requirements are flexible for small businesses, which limits considerably their access to loans. The regulations of the National Bank of Serbia only set the rules on the requirement of collateral from the perspective of risk weighted asset calculations and classification of assets. Thus, reliance on loans from commercial banks as a source of finance depends primarily on enterprise size. Despite

96 Crowdfunding is an alternative source of finance often used by both enterprises and individuals. It refers to the practice of funding a project/venture/cause by raising, as a rule, smaller amounts of money from many people/donors. It is most often conducted via online campaigns and platforms.

97 CEVES (2020), Enterprises in Serbia and Agenda 2030 – priorities, challenges and the COVID-19 crisis.

98 World Bank, Enterprise Survey, 2019, <http://www.enterprisesurveys.org>

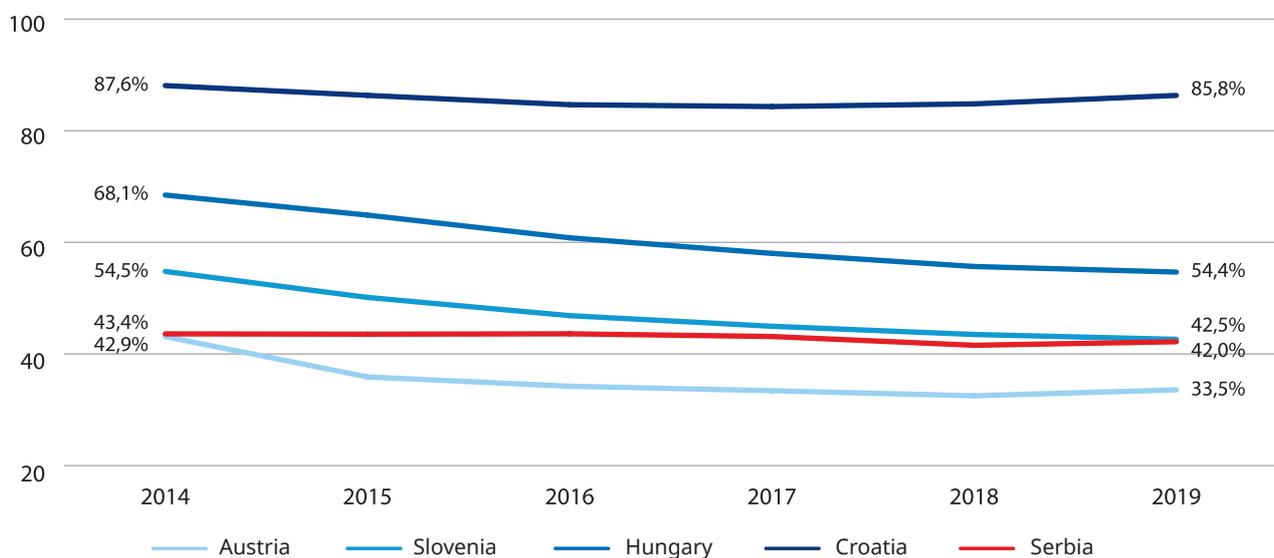
99 IMF (2017), MSME finance gap – assessment of the shortfalls and opportunities in financing micro, small and medium-sized enterprises in emerging markets.

100 World Bank Group (2020), Serbia Systematic Country Diagnostic Update.

relatively low collateral requirements, they remain relatively constraining for smaller businesses. In 2017, only 13 per cent of microenterprises used a loan, compared to 58 per cent of large ones.¹⁰¹ Positively, in 2019 around 41 per cent of loans required collateral (less than the global average of 58 per cent) and lower collateral requirements compared to many regional peers (101 per cent in Serbia compared to the 200 per cent global average).¹⁰²

The available domestic financing options for Serbian enterprises are weakly diversified. The indicator of domestic credit to private sector (percentage of GDP) refers to financial resources provided to the private sector, such as loans, purchases of non-equity securities, and trade credits and other accounts receivable that establish a claim for repayment. Between 2014 and 2019, the value for Serbia remained almost unchanged (Figure 15) with the average of 42.2 per cent – the second lowest performance (after Hungary – 35.3 per cent) among the five reference countries. However, when assessing overall financing options and resources available, it is important to consider foreign sources of finance as well. In Serbia, several international development finance institutions (European Bank for Reconstruction and Development, European Investment Bank, Council of Europe Development Bank) and donors support the local economy through various guarantee schemes and credit lines.

Figure 15. Domestic credit to the private sector (percentage of GDP)



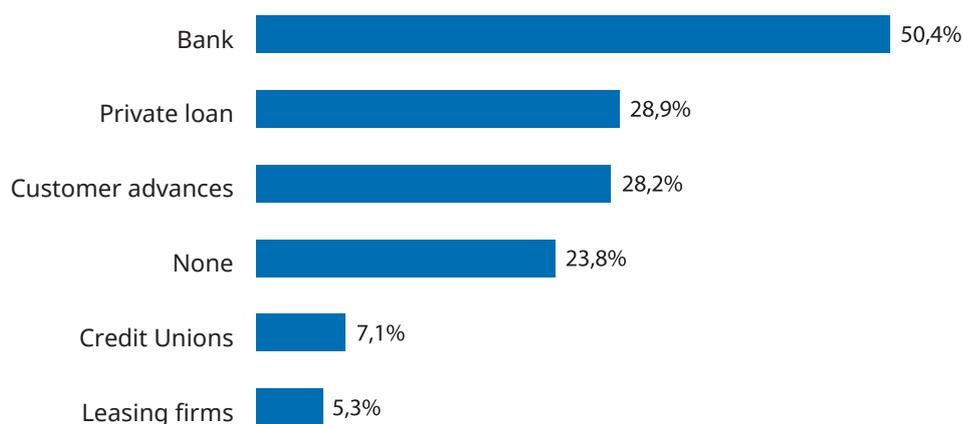
Source: World Bank, World Development Indicators.

The EESE survey reveals that enterprises resort most frequently to bank loans when they need external financing. Half of EESE respondents (50.4 per cent) used bank loans most frequently to fund their business operations, while other common sources include private loans (28.9 per cent) and customer advances (28.2 per cent) (Chart 23). However, focus groups participants confirmed that most enterprises relied mainly on their own reserves. For example, even when they were faced with severe liquidity shortage after the outbreak of the COVID-19 crisis, 55 per cent of enterprises resorted to their own reserves to cover for inconsistent/insufficient cash flow, although differences were significant among company sizes.¹⁰³

¹⁰¹ CEVES estimate based on data from the Serbian firm registry, which does not include around 200.00 entrepreneurs that are not obliged to submit financial reports.

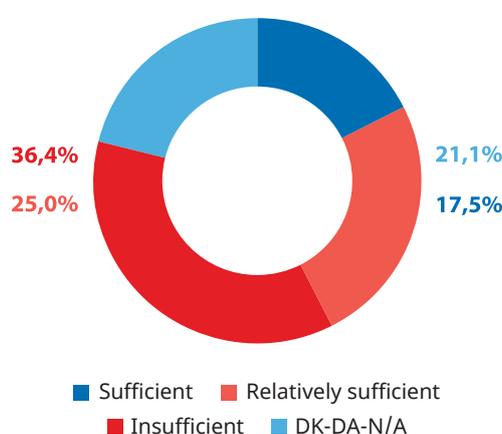
¹⁰² World Bank (2019), Serbia New Growth Agenda: Financing for Growth.

¹⁰³ SAE (2021), Navigating the COVID-19 Crisis: Evolving challenges, needs and expectations of Serbian enterprises, second edition.

Chart 23. What sources of (external) finance does your enterprise usually tap?


Source: EESE survey.

The MSMEs need advisory support to be able to apply for bank loans. More than a third of EESE respondents (36.4 per cent) reported that there was no sufficient support targeted at MSMEs, such as advisory services, to assist them in preparing bankable loan proposals (Chart 24). A quarter stated that there was sufficient support, while approximately a fifth had no knowledge about the issue. A recent study¹⁰⁴ found that weak financial management was the most significant obstacle for MSMEs to access financing. This includes difficulties to identify and clearly express financing needs, develop realistic business plans and present reliable financial statements.

Chart 24. Is there sufficient support targeted at MSMEs to assist them in preparing bankable loan proposals?


Source: EESE survey.

5.5 Information availability

Creditors in Serbia have access to quality information that facilitates their lending decisions. The World Bank credit information index, measures rules affecting the scope, accessibility, and quality of credit information available through public or private credit registries. The index ranges from 0 to 8, with higher values indicating the availability of more credit information, from either a public registry or a private bureau, to facilitate lending decisions. Between 2015 and 2019, Serbia and Austria had the highest score (7.0), which implies a rather favourable position

104 Center for Financial Reporting/ World Bank Group (2017), Small and Medium Enterprises: Financial Information as a Catalyst for Lending.

of their creditors (Table 2). Indeed, the infrastructure around credit history is solid.¹⁰⁵ A cadastre and a registration system for pledges over movable assets have been in place for several years and are largely functional and actively used by the local banking system, even though not fully available online. A privately run credit information bureau has been in place since 2004, covering 100 per cent of the Serbian adult population.

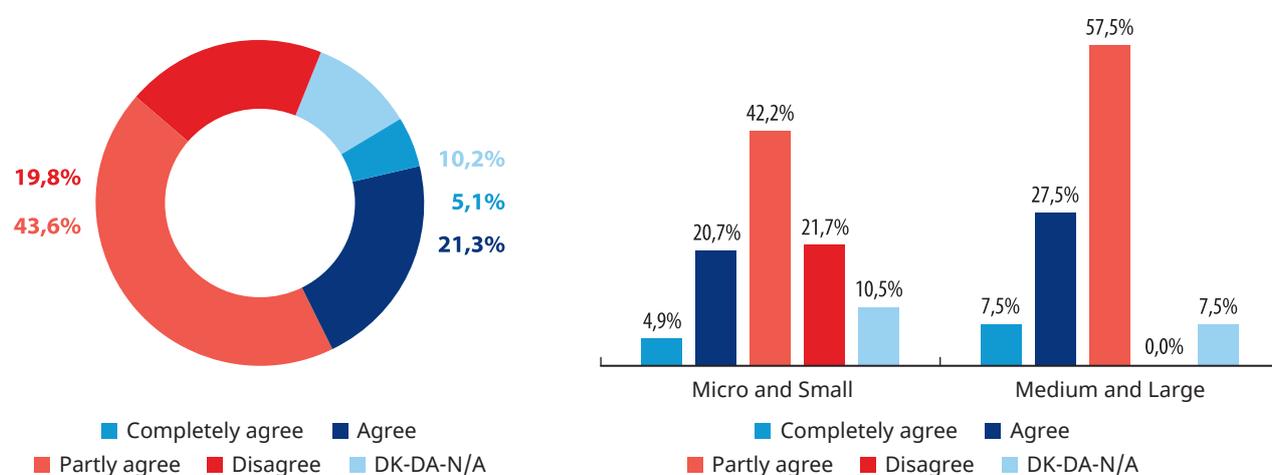
Table 2. Depth of Credit Information Index

Country	2015	2016	2017	2018	2019
Serbia	7,0	7,0	7,0	7,0	7,0
Austria	7,0	7,0	7,0	7,0	7,0
Croatia	6,0	6,0	6,0	5,0	6,0
Hungary	5,0	5,0	5,0	6,0	6,0
Slovenia	4,0	4,0	6,0	6,0	6,0

Source: World Bank, Doing Business Project.

The information on financial services is not well-distributed in the business sector. Some 43.6 per cent of EESE respondents only partly agreed that the information was well-distributed and a further 26.4 per cent agreed with the statement (Chart 25). On the opposite side, almost one fifth of respondents (19.8 per cent) did not perceive the information on financial services as being well disseminated to enterprises. There were some differences in responses provided by the representatives of small-scale and large-scale enterprises. About a quarter (25.6 per cent) of representatives of micro and small enterprises agreed that the financial services were well-distributed, compared to more than one third (35 per cent) of representatives of medium-sized and large enterprises that thought the same. In addition, 42.2 per cent of small-scale enterprises only partly agreed with the statement, compared to 57.5 per cent of large-scale enterprises. Most importantly, 21.7 per cent of micro and small enterprises disagreed completely with the statement, while no respondents among medium-sized and large enterprises shared a similar perception. About 40 per cent of participants in focus group discussions confirmed that they needed more information about available sources of finance and that they needed support in defining the adequate type of financial support for their businesses.

Chart 25. To what extent do you agree with the statement: “information on financial services is well-distributed in the business sector”? All enterprises (left) and enterprises by size (right)



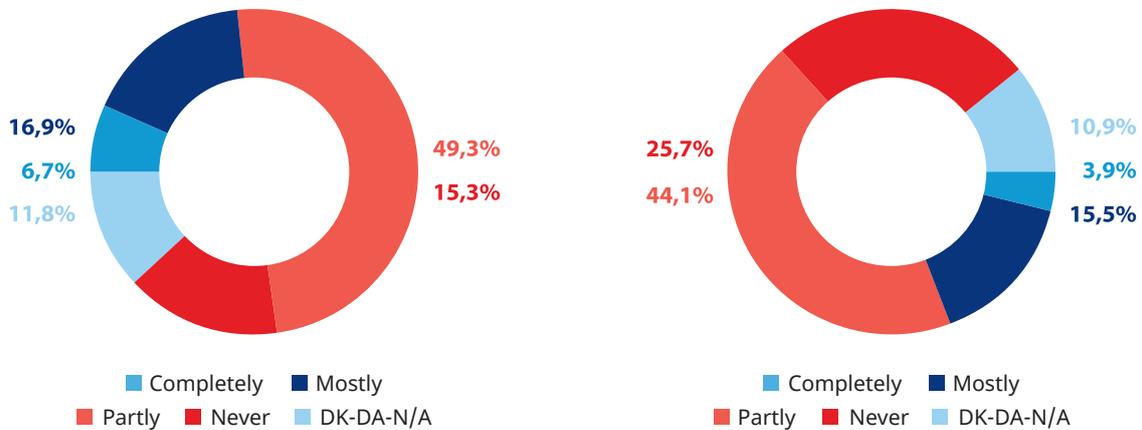
Source: EESE survey.

105 OECD (2019), SME Policy Index: Western Balkans and Turkey.

5.6 Adequacy of available financing sources

Overall, the available financial products and services are rarely fully adjusted to the actual needs of enterprises. Only 6.7 per cent of EESE respondents found such products and services as completely adequate to the needs of enterprises of varying sizes, while 15.3 per cent expressed an opposite view (Chart 26). A further 49.3 per cent stated that they were only partly adequate. The MSMEs were worse off, with only 3.9 per cent perceiving the available financial products as tailored to their needs and 25.7 per cent expressing disagreement with the statement. Focus group discussions revealed further that inadequacy applies not only to available financing sources but also to existing MSMEs support programmes (for instance, those provided by the Development Agency of Serbia or the Development Fund). Most participants never used them because they found them inappropriately tailored to their needs. Furthermore, these programmes have unclear eligibility criteria, complicated procedures and are non-transparent.

Chart 26. Are the financial products and services tailored to the needs of companies? All enterprises (left) and MSMEs (right)



Source: EESE survey.

6. Education, training and lifelong learning

6.1 Overview of legislative, policy and institutional framework

Driven by a strong commitment to EU integration, Serbia has developed a relevant legislative, policy and institutional framework to improve the quality and inclusiveness of education. Several important laws have been adopted in recent years to promote reforms in the education sector, with the laws on higher education (2017), adult development (2017), dual education (2017), national qualification framework (2018) and student organization (2021) being among the most important ones. A new strategy for Education Development in Serbia by 2030¹⁰⁶ was adopted in June 2020¹ aimed at further harmonizing the education policies with ongoing labour market trends and EU standards. The Ministry of Education, Science and Technological Development (MoESTD) is the main body responsible for designing and implementing the education policy in Serbia at all levels. MoESTD coordinates the work of two institutes: the Institute for Improvement of Education and the Institute of Educational Quality and Evaluation. The first is responsible for designing curricula for primary, secondary and adult education and drafting other technical documents. The second is responsible for quality assurance of primary and secondary education and for external school evaluations. It is also active in research and development and national and international assessments.¹⁰⁷

Serbia has made good progress in improving its skills framework. In 2018, the National Qualifications Framework for Serbia (NQFS) was adopted, for identifying, creating and classifying qualifications in accordance with demands of the labour market, lifelong learning, science and society in general.¹⁰⁸ The institutional infrastructure for the implementation of the framework has been put in place. Precisely, the Council for the National Qualifications Framework was established as an advisory body appointed by the Government, to make recommendations on the process of planning and developing human potential in accordance with public policies in the area of lifelong learning, employment, career guidance and counselling.¹⁰⁹ The council has the power to propose qualification standards for all levels of the framework. Serbia has also established the Qualifications Agency, which performs administrative and technical tasks, provides expert support for the Council and proposes quality assurance measures throughout the entire education system. Finally, sector skills councils have been set up as advisory bodies established on the principle of social partnership whose main function is to define the needs for qualifications in the labour market in Serbia. Overall, Serbia has a modern structure for skills governance. However, more efforts are needed to build the capacities of the newly established institutions and ensure proper coordination between them which is key to successful implementation of the NQES.¹¹⁰

The country has a solid base for upgrading its human capital and building a skilled workforce. Nearly all children participate in compulsory education, and participation rates at other levels, including technical training, are also very high. Participation at the upper secondary level has increased significantly over the past years and

¹⁰⁶ The document sets out two strategic objectives covering virtually the entire education system. The first objective focuses on improving the quality, fairness and accessibility of pre-university education (primary and secondary stage), while the second one focuses on higher education.

¹⁰⁷ The Ministry also receives expert advice and support from three autonomous councils: the National Education Council, the Council of TVET and Adult Education, and the Higher Education Council. Members of all three are appointed by the Government and represent stakeholders in their fields.

¹⁰⁸ Law on the national qualifications framework in Serbia (Official Gazette of RS 27/2018). It should be mentioned that the law on foundations of the education system, the law on higher education and the law on adult education are overall consistent with the National Qualifications Framework. More than that the law on adult education defines recognition of prior learning as one of the paths for acquisition of qualifications.

¹⁰⁹ The council includes decision makers in the education, employment, youth, economy, local self-government and health sectors as well as representatives from social partners, the Chamber of Commerce and Industry of Serbia, the National Employment Services, associations of secondary schools and higher education institutions, and civil society organizations.

¹¹⁰ Currently some of these institutions are operation below the expected level (for instance the Qualifications Agency is currently working with 60 per cent of its planned staffing levels).

is now about 87 per cent, higher than the Western Balkans and EU averages.¹¹¹ In addition, Serbia has a very high proportion of students in upper secondary technical vocational education and training (TVET): about 74 per cent of students enter TVET rather than general education, which is far above the EU average of 48 per cent.¹¹² There are two TVET options in Serbia: three-year and four-year. The latter offers the opportunity to transition to tertiary education later on. With the adoption of the law on dual education in 2017 and accompanying bylaws, Serbia started implementing a dual model for vocational education in 2019. Dual profiles allocate at least 20 per cent and at most 80 per cent of the total number of hours for vocational subjects to work-based learning. At 67.8 per cent, the participation rate in tertiary education in Serbia is close to the EU average.¹¹³ In terms of education outcomes, Serbia performs well compared to regional peers, as evidenced by its relatively strong performance on international student assessments, such as PISA, and its comparatively high enrolment and completion rates across all levels of education.¹¹⁴ Yet, further improvements are needed to align Serbia ratings to the EU averages on most international indicators.

Despite recent reforms, the education system is not yet adequately adapted to meet labour market needs.

The labour market recorded a further decrease in unemployment in 2020, reflecting in particular lower participation rates during the crisis.¹¹⁵ Prior to the crisis, employment rate reached 49.0 per cent, while the unemployment rate (among people age 15–64) fell to 10.4 per cent in 2019.¹¹⁶ As workers left the labour force, the rate of unemployment decreased further to 9.0 per cent in 2020, with a simultaneous slight increase in employment (49.1 per cent).¹¹⁷ However, unemployment rates for people under age 25 are about three times higher than for the overall labour force. Youth unemployment (age 15–24) decreased from 27.5 per cent in 2019 to 26.6 per cent in 2020 but remains high, while the rate of young people (age 15–24) not in employment, education or training (NEETs) increased to 15.9 per cent in 2020 from 15.3 per cent in 2019.¹¹⁸ Youth unemployment is highest among those with higher education, suggesting significant skills mismatches. A large share of young workers is engaged in low-wage occupations: 22.9 per cent, compared to the EU average of 17.2 per cent. Young workers are more likely to be low-wage earners (21.4 per cent) than those over age 30 (13.9 per cent).¹¹⁹ Furthermore, the employment rate of Serbian TVET graduates (age 20–34) is at 53.6 per cent, which is significantly lower than the employment rate of TVET graduates in the EU at 76.8 per cent.¹²⁰ Poor inclusion is a push factor in decisions to migrate abroad, which together with persistent long-term demographic pressures, pose a threat to the development potential of Serbia. On average, approximately 30,000–60,000 people per year left Serbia in recent years, one quarter of whom had completed higher education.¹²¹

Skills mismatches¹²² reflect outstanding weaknesses in the education system. The education system has been slow in adapting to changing labour market demand. The country's general secondary education curricula had not been updated for two decades until 2018, when elective subjects were introduced. Despite high TVET enrolment most schools use only partially updated curricula and lack special equipment to enable practical learning for

111 OECD (2021), Development Pathways, Multidimensional Review of the Western Balkans: Assessing Opportunities and Constraints. The total duration of compulsory education in Serbia is nine years. Children enter compulsory education at age 5.5 and leave it at age 14.5. It should be noted that socio-economic family background plays an important role in deciding whether students go to general or vocational programmes. Students from more favourable backgrounds are more likely to attend general schools. Evidence from PISA finds that there is a wide gap in learning outcomes across TVET and general education. Vocational students tend to have weaker literacy and numeracy skills than their peers in general education. In addition, socio-economically disadvantaged students in Serbia are more than five times as likely to attend a vocational upper secondary school, suggesting that current sorting mechanisms may reflect students' background more than their capability.

112 Ibid.

113 European Commission (2021), Serbia 2021 Report.

114 In particular, high school students achieve better test scores in Serbia than in neighbouring economies.

115 The economic crisis has led to a decrease in unemployment and an increase in inactivity because individuals who were unable to search for a job or to start working due to the virus spread prevention measures were classified as inactive.

116 SORS, Labour Force Surveys 2019 and 2020.

117 Ibid.

118 Ibid.

119 World Bank Group/Vienna Institute for International Economics Studies (2019), Western Balkans Labour Market Trends 2019.

120 European Commission (2021), Serbia 2021 Report.

121 O. Radonjić and M. Bobić (2020), Brain Drain Losses – a Case Study of Serbia, International Migration.

122 Skills mismatch is a discrepancy between the skills that are sought by employers and the skills that are possessed by individuals. Simply put, it is a mismatch between skills and jobs. This means that education and training are not providing the skills demanded in the labour market, or that the economy does not create jobs that correspond to the skills of individuals.

their students. Weak accountability in higher education results in a long and difficult transition to employment.¹²³ Funding of public universities is based on input-based budgets, not on performance. It is difficult for policymakers in Serbia to evaluate the effectiveness of policies and evaluate teacher and student performance, as information and monitoring and evaluation systems are underdeveloped. To monitor the implementation of the previous education strategy¹²⁴ MoESTD used a variety of indicators, which were, however, based mainly on system inputs and outputs, while indicators related to outcomes were relatively limited since Serbia does not have a regular national assessment of student learning.¹²⁵ The country must rely on international assessments (which are not specific to the Serbian context) and national examinations (which do not provide information on learning during the earlier years of schooling) in order to have comparable information about student learning. Moreover, even when information is available, the lack of staff in specialized public institutions with relevant experience hinders comprehensive system evaluation.¹²⁶

There is significant scope to improve the access to and quality of life-long learning in Serbia. Overall, participation in continuing vocational training/adult professional development is low in Serbia.¹²⁷ The Adult Survey of 2016 shows that 19.8 per cent of adults participated in some type of formal or non-formal education or training in 2016, slightly higher than in 2011 (16.5 per cent) but also well below the average of the EU Member States (45.1 per cent). The participation rate was highest among young adults (age 25–34), particularly among highly educated urban women. For the most part, training was work-related, took place during working hours and was paid for by employers. Less than a third of companies have regular contact with the education system and less than half provide training themselves.¹²⁸ Life-long learning for continuing professional development can help address skills mismatches after the completion of formal education, including addressing the challenges of long-term unemployment. Currently five centres for lifelong learning which offer continuing vocational training opportunities have been established at universities, as well as a number of training courses and programmes. Lifelong learning participation slightly dropped to 3.7 per cent in 2020 from 4.3 per cent in previous years, being particularly low among low-skilled adults (0.3 per cent) which is far below the EU average (9.2 per cent).¹²⁹

6.2 Education indicators

Government spending on education is lower in Serbia than in reference countries (Table 3). Numerous studies have shown that countries that spend more on education may expect better test scores and higher graduation rates, including among students from lower income families.¹³⁰ The World Bank measures government spending on education as a percentage of GDP, taking into account current and capital public expenditures on education, as well as government subsidies to private education institutions. Between 2014 and 2017, Serbia spent much less on education than reference countries. For instance, in 2017, Serbia spent 3.7 per cent of GDP on education, which is significantly lower than expenditures in the best performing countries, namely Austria (5.4 per cent) and Slovenia

123 The time required for a young person in Serbia to find a first stable employment is two years compared to 6.5 months in the EU.

124 The previous Strategy for Education Development in Serbia was adopted in 2012 and expired in 2020.

125 Prior to 2018 Serbia had not conducted a national assessment since 2006. The Government plans to develop a new national assessment, building on a pilot instrument that was conducted in 2018. These include the introduction of an education management information system that will be linked to the Central Registry of Statutory Social Insurance and, thus, enable the monitoring of graduates' performance in the labour market and, in turn, help design better education policies to meet labour market needs.

126 MoESTD Report (2018). The similar goes for capacity challenges obstructing the work of specialized institutes that provide technical expertise or design certain policies, such as the Institute for Education Quality and Evaluation or the Institute for Improvement of Education. While indisputably having technical expertise, they both lack staff and funding. For example, in 2017, less than half positions in the Institute for Education Quality and Evaluation were filled (15/33), with few employees skilled in quantitative research, or experienced in the fields of statistics, psychometrics and survey design.

127 European Commission (2019), Serbia 2019 Report.

128 SORS (2018), Adult Education Survey, 2016. The Adult Education Survey is administered in a five-year cycle. The last survey was conducted in 2016.

129 It should be also highlighted that the education strategy adopted in 2012 (which expired in 2020) envisioned that the participation of adults in education would increase from 3 per cent in 2008, to 7 per cent in 2020. Since 2012, however, the percentage of people between age 25 and 64 in Serbia engaging in lifelong learning has hovered around 4 per cent.

130 Several recent studies that employ larger datasets and use quasi-experimental methods allowed for more credible causal claims. Even though they were conducted in the United States, it is expected that effects could be even greater in low/middle income countries. See C. Kirabo Jackson (2020), "Does School Spending Matter? The New Literature on an Old Question" An Equal Start: Policy and Practice to Promote Equality of Opportunity for Children

(4.8 per cent). Spending on education in Serbia is below the EU average of 4.7 per cent.¹³¹ Overall, government spending on education decreased from 3.9 per cent of GDP in 2014 to 3.6 per cent in 2018. In 2019 public spending on education stood at around 3.3 per cent of GDP. A recent evaluation of the education system pointed to chronic underfunding.¹³² The level of public expenditure on education, especially at the secondary level, has an important impact on education outcomes in Serbia. Overall public expenditure on secondary education is relatively low compared to neighbouring and European economies, despite similarly high enrolment rates at the secondary level. Low secondary education spending may reflect the fact that these programmes are still based mainly on theory, representing another gap at the secondary level.

Education outcomes are relatively poor but improving in Serbia. The education dimension of the Human Development Index is an important indicator. It is calculated as average of mean years of schooling (of adults, >25 years of age) and expected years of schooling (of children) – each receiving 50 per cent weighting for a total index value between 0 and 1. As shown in Table 3, between 2014 and 2019, Serbia had the lowest education index score compared to the reference countries, which confirms previous results. With an index value of 0.78 in 2019, it fared slightly worse than Croatia (0.81) and Hungary (0.82), while remaining quite behind the best performing Slovenia (0.91). However, reforms in the education system led to some improvements between 2014 and 2019, and Serbia increased its education index score more rapidly than any other comparator country.

Table 3. Education indicators

Index	Country	2014	2015	2016	2017	2018	2019
Government spending on education (percentage of GDP)	Austria	5,5	5,5	5,5	5,4	n/a	n/a
	Slovenia	5,3	4,9	4,8	4,8	n/a	n/a
	Hungary	4,6	4,5	4,7	4,7	n/a	n/a
	Croatia	n/a	n/a	n/a	n/a	n/a	n/a
	Serbia	3,9	3,8	3,6	3,7	3,6	n/a
Education index (0–1)	Austria	0,85	0,86	0,86	0,87	0,87	0,87
	Slovenia	0,90	0,90	0,90	0,90	0,90	0,91
	Hungary	0,82	0,82	0,82	0,82	0,82	0,82
	Croatia	0,80	0,80	0,80	0,80	0,80	0,81
	Serbia	0,75	0,75	0,78	0,78	0,78	0,78

Source: World Bank Databank and Human Development Reports.

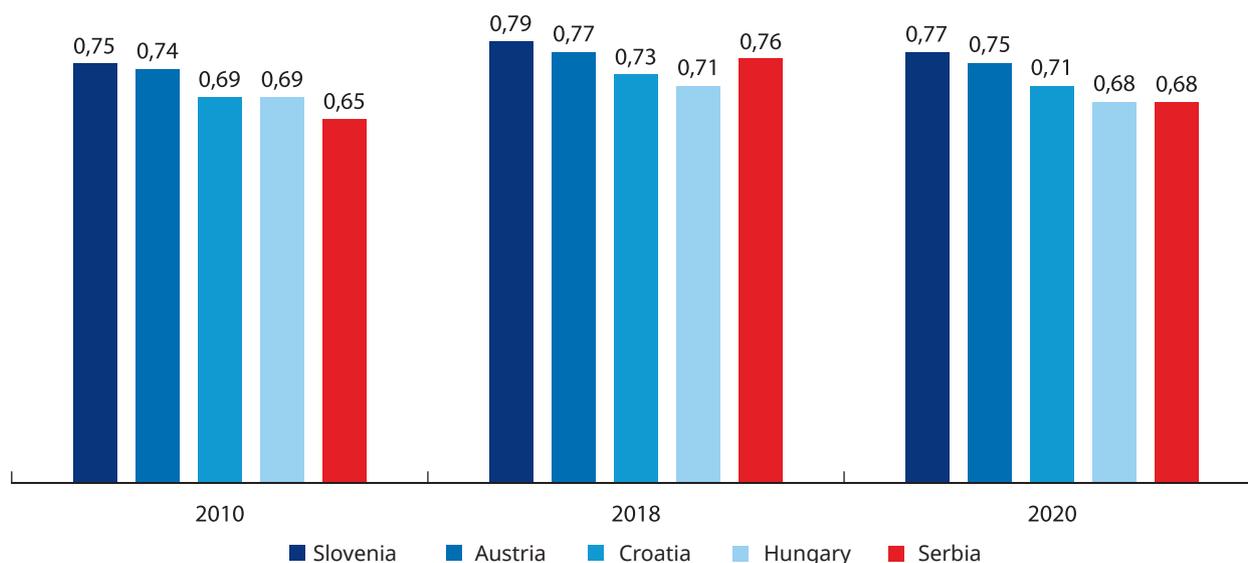
Serbia is the worst performer among reference countries in the Human Capital Index (Figure 16). The Human Capital Index measures the human capital that a child born today can expect to attain by 18 years of age, given the risks of poor health and poor education prevailing in their country. The index incorporates measures of different dimensions of human capital: health (child survival and adult survival rates) and the quantity and quality of schooling (expected years of schooling and international test scores). The 2020 update of the index incorporates the most recent available data for 174 countries. Figure 16 shows three distinct periods – 2010, 2018 and 2020.¹³³ In 2020, Serbia scored worse (0.68) than all reference countries, except for Hungary (which also scored 0.68). This means that a Serbian child born today is expected to reach 68 per cent of his/her full potential by age 18, while those born in Slovenia, for example, would have reached 77 per cent.

¹³¹ European Commission (2021), Serbia 2021 Report.

¹³² OECD (2021), Development Pathways, Multidimensional Review of the Western Balkans: Assessing Opportunities and Constraints.

¹³³ Data used for calculating 2020 HCI were the data available before the pandemic struck. Therefore, the exact impact of the pandemic remains unknown and 2020 HCI becomes a baseline for future comparisons.

Figure 16. Human Capital Index

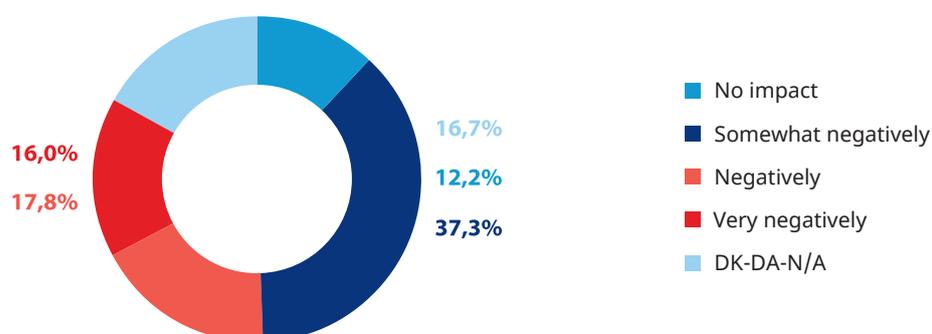


Source: Human Capital Index 2020, Update – Human capital in the Time of COVID-19.

6.3 Skills conundrum

Skills shortages¹³⁴ are becoming an increasingly substantial obstacle to doing business in Serbia. A significant share of EESE respondents (33.8 per cent) assessed skills shortages as having a negative or extremely negative impact on their enterprises, whereas 37.3 per cent perceived the impact as somewhat negative (Chart 27). The EESE survey findings resonate with the employer survey conducted by the National Employment Services in 2017, according to which 29.3 per cent of enterprises reported hiring problems, mainly due to skills shortages, which was an increase from 14 per cent in 2014. Furthermore, according to the 2019 World Bank enterprise survey, inadequate access to skilled staff was rated as the second most frequently cited obstacle to doing business in Serbia. The STEP Employer Survey for Serbia revealed that difficult access to skilled labour affects dynamic enterprises in particular.¹³⁵ Enterprises that have made a technology-related innovation in the past three years tend to have higher growth prospects and are more likely to hire, but more of them cite the lack of skills among applicants as a problem.

Chart 27. How do skills shortages affect the development of enterprises?



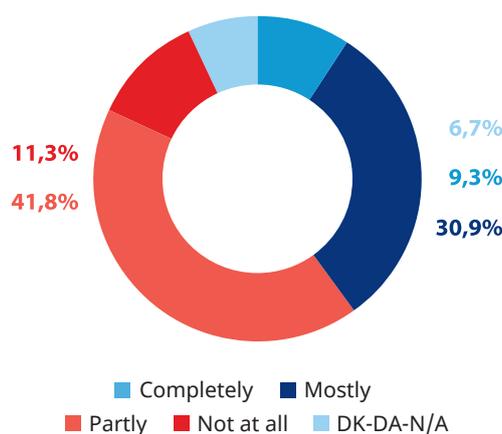
Source: EESE survey.

¹³⁴ Skill shortages do not imply skill mismatch if vacant jobs remain unfilled but can create skill mismatch if employers unable to find the skills they need end up recruiting workers who are under-skilled for a specific job. The term “skill gap” is often used when the skill levels of the existing workforce are insufficient to meet the requirements of companies.

¹³⁵ World Bank (2018), STEP Employer Survey, Serbia, 2015–2016.

The EESE survey shows that vocational and higher education institutions do not sufficiently equip students with job relevant skills. Only 9.3 per cent of respondents were of the opinion that students were fully equipped for the labour market, and a further 30.9 per cent found them as mostly prepared for employment (figure 6.3). In contrast, a further 53.1 per cent assessed students as being only partly prepared or completely unprepared to meet the needs of enterprises. These survey findings were further confirmed by focus group discussions. In addition to job-specific skills, focus group participants noted the importance of socio-emotional skills (resilience, teamwork, stress resistance and reliability) which are becoming increasingly important, but which are not well integrated into education curricula.

Chart 28. Do vocational and higher education institutions equip students with job-relevant skills?

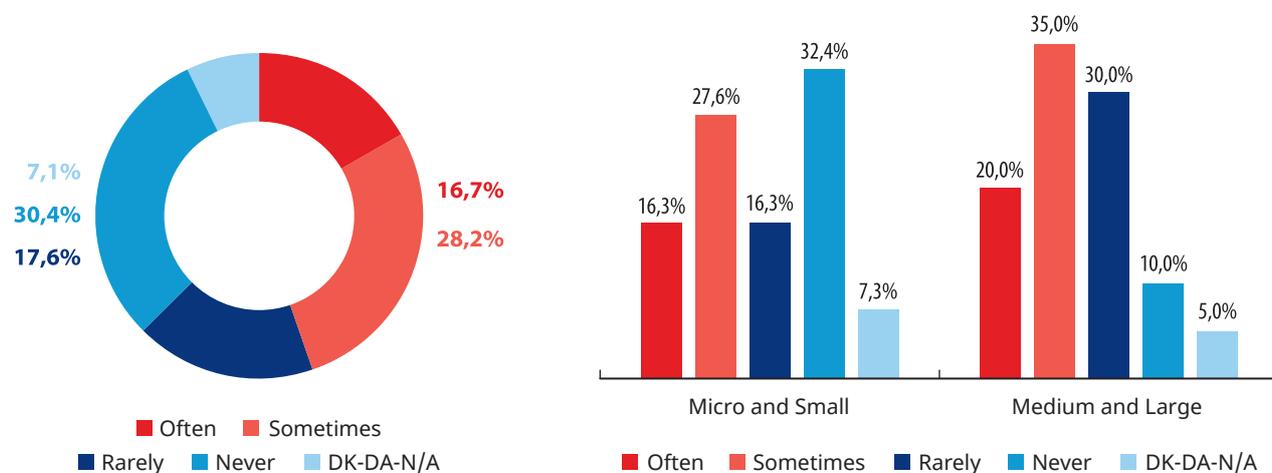


Source: EESE survey.

Most of the surveyed enterprises that were hiring had difficulty in finding workers with certain skills, especially highly skilled workers. About 45 per cent of responding enterprises reported having constant or frequent difficulties in recruiting workers with the right skills, with the problem being more acute among medium-sized and large enterprises (55 per cent) (Chart 29). A further 17.6 per cent experienced only occasionally such difficulties while 30.4 per cent reported having had no difficulties in recruiting skilled workers. Focus group participants also mentioned that further aggravating the situation is the problem of over-qualification,¹³⁶ especially with regard to university graduates. Indeed, employers pay an estimated wage premium of 7.9 per cent for highly educated workers, meaning that wages were approximately 7.9 per cent higher for each year spent in higher education. However, higher education diplomas do not necessarily guarantee that graduates have the needed skill set. In general, focus group participants were of the opinion that the skills of TVET graduates are slightly more relevant than those of general education graduates.

¹³⁶ Over-qualification/over-skilling may result from an oversupply of university graduates and/or from skills gaps among young graduates if they are not acquiring the technical and soft skills employers need, and weaknesses in the education-to-work transition. Graduates' first work experience may thus be in jobs requiring a much lower formal education level. It may happen that a person is simultaneously overqualified and underskilled.

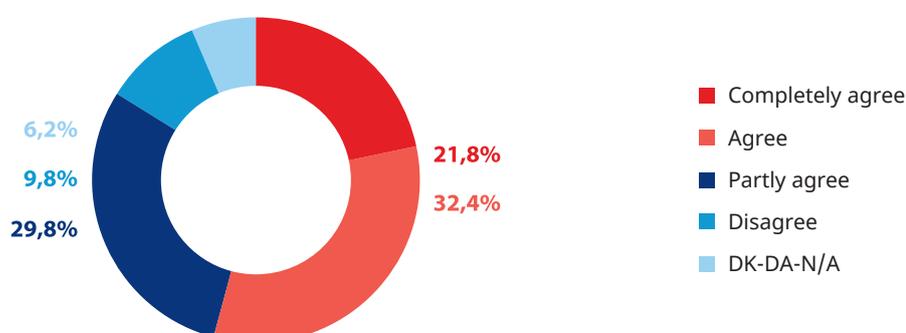
Chart 29. Has your company experienced difficulties in recruiting employees with certain skills in the past three years? All enterprises (left) and enterprises by size (right)



Source: EESE survey.

More than half of EESE respondents assessed the lack of collaboration between businesses and relevant stakeholders as a major impediment to developing the right skills mix at the right time. Without collaboration among decision-makers, business sector representatives, educational institutions and other stakeholders, it is difficult to understand (and anticipate) enterprise needs and consequently design and implement effective education policies and programmes. Despite Government's latest efforts to promote greater cooperation and coordination in the field of education, 54.2 per cent of the EESE respondents find the lack of coordination between enterprise needs and the offer of the education system as a significant barrier to building and maintaining a skilled workforce, with a further 29.8 per cent partially supporting the statement (Chart 30). One of the programmes launched by the National Employment Services – My First Salary– was mentioned during the focus group discussions as having a good impact on employment.¹³⁷ A number of respondents who took part in it reported having mentored and later permanently hired selected candidates. In addition, participants reinforced the stringent need for systematic coordination and collaboration in shaping the education offer to the actual enterprise needs. Furthermore, employers mentioned the need to anticipate future skills, especially taking into account the rapid pace of technological development.

Chart 30. To what extent do you agree with the statement that “a significant barrier to developing and maintaining a skilled workforce is the lack of coordination between the needs of enterprises and the offer of the education system”?

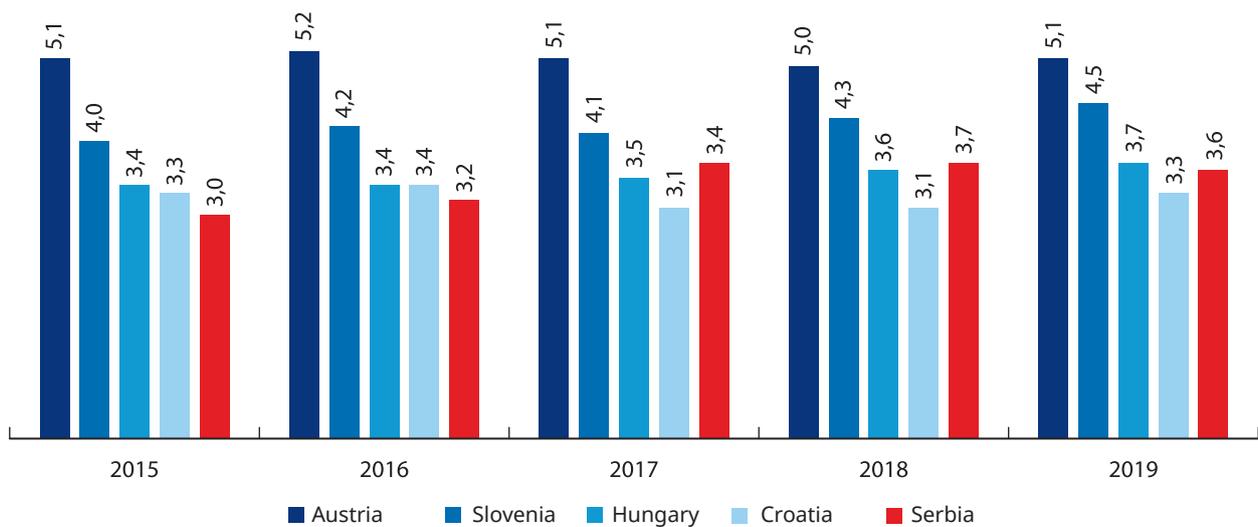


Source: EESE survey.

¹³⁷ The programme was launched in the second half of 2020 and pays a monthly cash benefit to young people employed through this programme: 20,000 dinars to those with secondary education, and 24,000 dinars to those with higher education. It also covers an allowance in the case of injury or occupational diseases. The programme targets employers from disadvantaged municipalities in particular.

Serbian enterprises are becoming increasingly aware of the need to continually invest into their human resources. The indicator on the extent of staff training, calculated by the World Economic Forum, shows a slow but gradual increase in investments made by Serbian enterprises in staff training. Figure 17 shows that in 2019, Serbia (3.6) was far behind Austria (5.1) and Slovenia (4.5) but close to Hungary (3.7) and above Croatia (3.3). Focus group participants expressed readiness to invest in staff development. According to them, most of the training offered over the past two years was job-related. Interestingly, employers showed readiness to invest into boosting workers' socio-emotional skills as these are becoming increasingly important. However, they expect much greater support from the Government when it comes to life-long learning programmes, which they find underdeveloped. They also expressed particular support for dual education programmes.

Figure 17. Extent of staff training



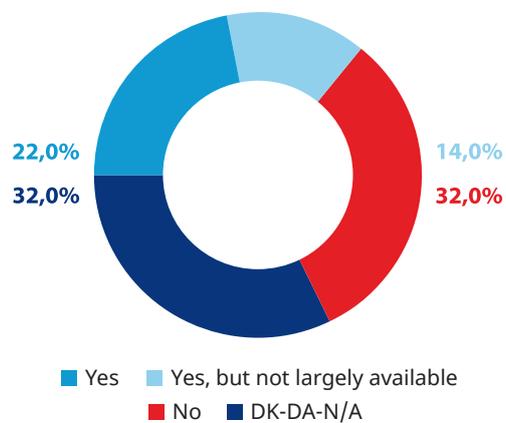
Source: World Economic Forum Executive Opinion Survey.

Note: With the indicator, extent of staff training, the World Economic Forum Survey asks business leaders to provide their expert opinions on the following: "The general approach of companies in your country to human resources is: to invest little in training and employee development (1), to invest heavily to attract, train, and retain employees (7)".

The EESE survey shows that opportunities for continuing vocational education and training are not broadly available in Serbia (Chart 31). About 64 per cent of enterprises were convinced that there were no government employment and training programmes available to address skills shortages, or they did not know about them. Of 34 per cent of enterprises that were aware of government programmes, 14 per cent noted that they were difficult to access. Indeed, participation in continuing vocational training is low in Serbia. The Adult Survey of 2016 showed that almost half of respondents (47 per cent) wanted to participate in adult learning but could not owing to the costs of education/ training, family reasons, scheduling (such as overlapping with working hours) and lack of suitable training.¹³⁸ From an employer's perspective, less than a third of companies have regular contact with the education system. These low participation trends are thought to reflect a lack of capacity for skills assessment as well as limited knowledge of the returns of investing in training.

¹³⁸ SORS (2018), Adult Education Survey, 2016.

Chart 31. Are there government employment and training schemes available that could assist with skills shortages?



Source: EESE survey.

Recommendations

The Serbian Association of Employers (SAE) proposes the following recommendations to the Government with the aim to further improve the business environment, increase enterprise resilience and accelerate economic and social recovery.¹³⁹

Good governance

Strengthen the effectiveness, efficiency and accountability of public administration: First and foremost, Serbia needs to accelerate the completion of public administration reform. The lines of accountability between various public administration institutions need to be clearly defined to avoid overlapping functions and unclear reporting lines. Institutional coordination needs to be strengthened to improve the implementation and monitoring of ongoing reforms. More effective mechanisms need to be put in place to ensure a strong quality control role for the Public Policy Secretariat to allow for the effective implementation of the law on the planning system. The public service sector needs to increase its efficiency by reducing red tape, increasing transparency and strengthening e-governance, including e-services for businesses. It is equally important to strengthen the integrity of the civil service by pursuing professionalism and merit-based recruitment and reducing the excessive number of acting senior management posts. Last but not least, a unified, comprehensive and transparent system needs to be put in place for capital investment planning and management.

Enhance government transparency and accountability in combating corruption and 'rent seeking' practices: Effective mechanisms need to be put in place to prevent bribery and other forms of corrupt payments being imposed on enterprises when applying for permits and licenses or during inspections. One of the key steps towards ensuring more effective anti-corruption mechanisms are the amendments to the relevant legal provisions to firmly preserve the independence of the judiciary by (inter alia) reducing the political influence on the selection and appointment of judges. Furthermore, the legal framework on whistleblowers needs to be improved. The Government needs to ensure the protection of whistleblowers and investigate allegations in high corruption cases, in order to strengthen trust in anti-corruption institutions. Public procurement is one of the areas that is most prone to corruption. It is the duty of the government to provide all qualified bidders with a fair opportunity to enter the bidding process and limit the abusive use of exceptional procedures. There is also an urgent need to adopt a new anti-corruption strategy and action plan and to establish an effective coordination mechanism to effectively address corruption.

Social dialogue

Recognize the role and increase the influence of the tripartite Social and Economic Council (SEC) over policy and law-making: The Government should fully acknowledge the role of SEC as the main national tripartite advisory body and consistently involve social partners at an early stage of policy and law-making. To give greater recognition to SEC, the Government should ensure an appropriate representation at SEC meetings and discontinue the current practice of frequently replacing key ministers with their deputies. At the same time, the Government should refrain completely from bypassing the SEC debate and using emergency procedures to adopt legislation falling under SEC competence. The Government and parliament should require that SEC recommendations accompany all bills submitted to parliament for discussion. Following the practice of some EU countries (France, Italy, Portugal and Romania) policymakers should consider enshrining the SEC in the constitution of Serbia to show their true commitment to social dialogue.

¹³⁹ SAE will develop a detailed action plan with specific indicators based on these priorities.

Considerably strengthen the technical capacity of economic and social councils at all levels: The Government should increase funding and human resources to capacitate the secretariats and specialized committees of the economic and social councils to deliver high quality outcomes and ensure their regular access to relevant external expertise (academia, research institutes, think tanks, and so on). Building adequate technical capacity is crucial for the social and economic councils to be able to prove their effectiveness and contribute meaningfully to policy and law-making process. Well-functioning social dialogue institutions are crucial to tackling the impact of the protracted COVID-19 crisis and defining joint solutions for an inclusive and sustainable recovery.

Enabling legal and regulatory framework

Improve the predictability of the business environment and quality of regulations: The predictability of the business environment needs to be considerably improved to allow businesses to adapt their operations within the time provided to comply with the new laws and regulatory changes. Extensive consultations with the business community, including through the social and economic councils, should be held well ahead of regulatory changes, and further guidance on the interpretation of the newly adopted laws and regulations should be largely made available for all businesses to use. Currently, businesses have to invest considerable resources and hire external consultants to stay on top of legislative changes, which is particularly challenging for smaller enterprises. Further efforts need to be invested in improving the quality of regulations to ensure they are clear and easy for enterprises to follow. Furthermore, the legislative changes adopted as part of the EU accession process should be consistent. The adoption of secondary legislation that guides the operational enactment of primary legislation should be adopted without delays to avoid uncertainty and contradictions.

Reduce the administrative and regulatory burden on business: The costs of doing business need to be further optimized to support enterprise development and encourage entrepreneurship and start-ups. Labour taxes (in particular social security contributions) and payments originating from indirect taxation, with parafiscal charges being the most pressing, need to be reviewed and reduced. In addition, tax administration should be considerably simplified and the average number of tax payments per year (33) should be reduced by at least half. Although the number of payments per year in Serbia has already been reduced by half since 2014 (from 67 to 33), the number remains well above that of comparable peers, namely Austria, Hungary and Croatia, with 11, 12 and 12 payments respectively. Furthermore, the Government should accelerate the set-up of one stop shops (there are currently one stop shops in 14 municipalities and cities) as a single entry point to authorities. One-stop shops should provide several integrated functions, such as starting a business, post-registration formalities with tax authorities, as well issuance of documents, licenses and permits.

Fair competition

Ensure competitive neutrality in the enforcement of competition rules: Authorities need to ensure a balanced regulatory treatment so that competing enterprises are subject to equivalent competition rules, irrespective of their ownership or legal form, and that the enforcement of those rules does not discriminate between state-owned enterprises, foreign investors and domestic private businesses. There is an urgent need to resume work on drafting a new law on the protection of competition and further align the legislative framework on state aid rules with the EU acquis. The institutional capacity of the Commission for the Protection of Competition (CPC) needs to be further strengthened and administrative procedures applied by the CPC need to be harmonized with the latest amendments to the law on general administrative procedure. It is very important to increase the capacity and specialization of the judiciary to deal with complex competition cases, which have reported very modest results so far.

Ensure a level playing field for all business by reducing the size and distortiveness of state aid for privileged state-owned enterprises (SOE) and large foreign investors and ensuring more transparency in public procurements. The findings of this report indicate that domestic businesses, in particular the micro, small and medium-sized enterprises (MSMEs), feel discriminated against compared to the SOEs (some of which are inefficient and provide low overall returns on the state's investment) and foreign competitors which benefit from preferential treatment by the Government. State aid and subsidies should be equally available and fairly distributed to domestic

businesses to support their growth and incentivize them to invest in the economy. In the area of public procurement, the Government needs to urgently review the new law on special procedures for linear infrastructure projects adopted in 2020, under which it can exempt linear infrastructure projects of 'special importance for the Republic of Serbia' from the application of public procurement rules and is empowered to select a strategic partner in circumstances deemed as urgent. This law not only circumvents national legislation but also the EU rules and standards.

Support the formalization of enterprises: This process will require coordination among state authorities and the implementation of a set of complex policy measures, such as further reforms of the businesses environment (including lowering the entry costs and compliance costs, including taxes, fees and social contributions). For instance, the current tax wedge is still disproportionately high for people with low salaries and should be lowered in order to support the formalization of employment. Enterprises could be also supported to formalize through incentives while improving the oversight and sanctioning for illegal business operation.

Access to finance

Improve the MSME access to bank loans, including through strengthened national credit guarantee schemes: Financing for micro-, small and medium-sized enterprises (MSMEs) in Serbia is heavily bank-centric, while non-collateral-based funding remains limited. The banking sector in Serbia is mostly comprised of two types of banks – large liquidity-rich banks mainly focused on larger enterprises and smaller MSME oriented banks with less abundant liquidity. In this sense, the most effective economic support measures would include providing incentives to large banks to enter the MSME market and additional liquidity to smaller banks to allow for MSME credit expansion. Moreover, an effective credit guarantee scheme can help companies fulfil the collateral requirements and provide risk sharing guarantee to the banks.

Broaden Government support programmes and eligibility criteria for MSMEs: The Government should review and customize its credit policies and decisions for support programmes to better respond to the MSMEs needs. Such programmes should be oriented towards supporting start-ups or early-stage high-risk innovative businesses (apart from those offered by the Development Agency of Serbia and Innovation Fund). Likewise, the programmes should be better targeted at MSMEs with good growth potential rather than those that generally fall under the eligibility criteria. It is equally important to establish an online service for obtaining necessary information related to existing programmes. In addition, government agencies should organize regular campaigns and workshops where participants would have the opportunity to learn first-hand about all available financing options.

Diversify the financing options for MSMEs, especially for microenterprises, entrepreneurs and start-ups: Access to a sufficiently broad range of financing instruments is crucial for obtaining the type and volume of financing that best suits the specific needs of MSMEs at every stage of the enterprise life cycle. Alternative sources of finance are particularly valuable for and used by microenterprises, entrepreneurs and start-ups that are currently underserved by the banking sector. Alternative financing mechanisms for MSMEs and innovative start-ups need to be further developed to offer adapted modes of finance, such as microfinance, crowdfunding, business angels and venture capitals, eventually leading to development of capital markets. More efforts are needed to further develop and support the uptake of available alternative financing options, while developing, at the same time, an appropriate legal framework for those that are not yet regulated, such as crowdfunding and micro-crediting.

Develop well-targeted advisory services to support enterprises to access financing and improve financial management: Weak financial management is one of the most significant obstacles for MSMEs to access financing. Among others, this includes difficulties to identify and clearly express financing needs, develop realistic business plans and present reliable financial statements. One way forward is to intensify the delivery of available advisory services of the Serbian Development Agency and target the MSME sector, in particular. It is also important to ensure an adequate environment for the development of competitive private business service providers.

Education, training and life-long-learning

Accelerate the reform of the education system at all levels: The current funding mechanism of vocational and higher education institutions need to be reviewed to make it more performance oriented rather than input based. The change in the funding approach will increase the competition between education institutions, which will contribute to an improvement in the quality of education. For policymakers to be able to make informed decisions there is an urgent need to strengthen the collection and management of education data. The education and labour market databases should be linked (as planned by the Government), so information on education inputs, processes and outcomes can be more effectively analysed and decision-making can be more strategic to improve the quality and relevance of education. Social partners should be more effectively included in the development of education policies, as well as in the shaping of technical and vocational education and training (TVET) and continuing vocational education and training.

Implement more comprehensive skills needs anticipation, including at sectoral level, that should benefit from the active participation of employers: It is of critical importance to have in place a well-functioning system that will help policymakers to understand the type of skills likely to be in demand in the future so that education and training programmes can be adjusted to align supply with demand. The outcomes of such analysis need to be shared transparently, and mechanisms need to be found to translate them into actions (for example, adapting occupational standards, qualifications, curricula, exams, teacher training and so on).

Introduce state-supported incentive schemes for enterprises that invest in staff development and training: Increasing the capacities of enterprises to carry out in-company training and staff development is crucial, especially for MSMEs. The incentives should, in particular, aim at providing re-training and up-skilling for low-skilled workers (including those in flexible employment schemes) with a focus on youth, women and other disadvantaged groups. Policymakers may consider a number of ways to do this. One option could be the provision of training grants (cash reimbursements) to help to cover the cost of training. Training assistance could be financed through payroll levies and tax credits. A payroll-based levy would allow companies to choose to either spend a specific percentage of their payroll on training or contribute that percentage to a state-initiated training fund. A training tax credit typically equals a percentage of an employer's approved training cost and can be used to offset the taxpayer's income tax. The most suitable models should be defined in close collaboration with the private sector.

Develop a national database of internships to match students with internship opportunities: Internships are not sufficiently integrated into the educational programmes in Serbia, and students are left without hands on work experience until graduation. This entails a long and difficult transition to employment while employers are faced with major difficulties in finding workers with the right skills. An internship matching programme would allow students to apply for internships at participating employers and employers would be able to see if students have the qualifications and skills they are seeking, making it easier to determine if applicants are the right fit.

Improve access to and quality of life-long learning: The Government should explore novel ways of providing continuing vocational training. Therefore, developing instruments such as training vouchers, individual learning accounts and individual savings accounts for training would strengthen people's awareness of the availability and importance of learning activities. Training vouchers should provide individuals with direct subsidies for training purposes, often with co-financing from the individual. Learning accounts are more complex and need to be well designed and targeted in order to produce results. Such accounts are 'virtual' in that resources are only mobilized if training is undertaken, and training rights are accumulated over time. Individual savings accounts for training are 'real' in that resources for training accumulate over time and unused resources remain the property of the individual and may be used for other purposes (for example, retirement).

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Annex: Demographics of the survey sample

The survey sample was representative of the national enterprise distribution in 2018 in terms of size, sector, and regional distribution, when there were about 102 thousand active companies and 272 thousand active entrepreneurs. Enterprises included in the survey were selected randomly from SORS databases. Demographic characteristics of the survey sample are provided in this annex.

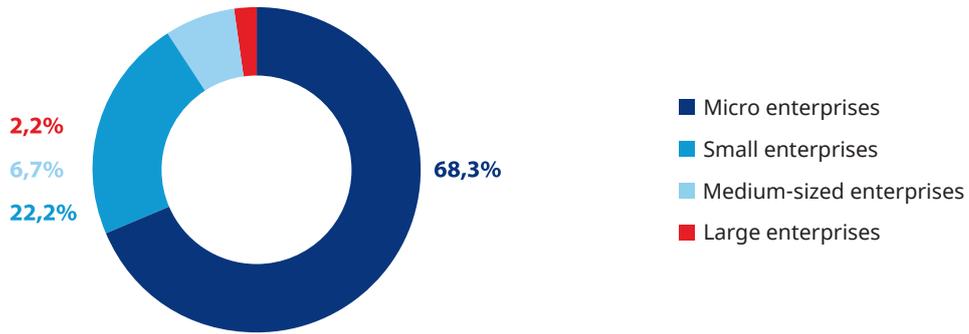
Table 1A. Distribution by sector

Sector	Survey sample	
	Number	Percentage
Manufacturing	147	33
Wholesale and retail trade; repair of motor vehicles and motorcycles	127	28
Administrative and support service activities; professional, scientific and technical activities	99	22
Transport and storage	19	4
Construction	34	8
Information and communication	8	2
Accommodation and food service activities	11	2
Real estate activities	5	1
Total	450	100

Table 2A. Distribution by gender of respondents

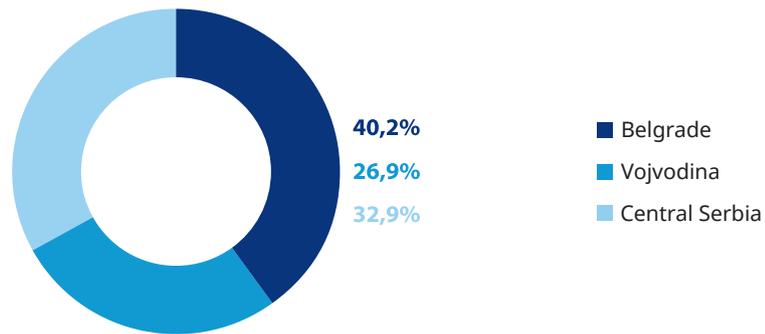
Sex	Number of respondents	Percentage
Male	323	71.8
Female	127	28.2
Total	450	100

Chart 1A. Distribution by enterprise size



Note: According to the law on accounting from 2018, there are four enterprise sizes based on average number of employees, business income and average value of business assets: micro (up to ten employees, income of €700,000, and €350,000 in assets); small (11–50 employees, income of €700,000–€8,800,000, and assets of €350,000–€4,400,000), medium-sized (51–250 employees, income of €8,800,000–€35,000,000, and assets of €4,400,000–€17,500,000) and large (those that exceed two of the three criteria for a medium-sized enterprise).

Chart 2A. Distribution by region



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