

## **Competitiveness of Business Environment of the Western Balkan Countries**

**Zoran Najdanović**

EFFECTUS University College for Finance and Law, Croatia  
*zoran.najdanovic@gmail.com*

**Marijana Žiravac Mladenović**

University for Business Engineering and Management, Faculty of Economics, Bosnia and Herzegovina  
*marijana.mladenovic@univerzitetpim.com*

**Natalia Tutek**

Croatian Post Bank, Croatia  
*natalija.anic@gmail.com*

*Abstract.* Economic competitiveness of the Western Balkan countries is uneven. Concept of competitiveness of the country is a source of important information enabling investors to perceive potentials of their future investment returns. Poor ranking of a country signals to potential investors to take additional measures of caution about their investing intentions. Beyond that, the level of competitiveness of an economy has a material role in its economic growth and development.

The main research objective of this paper is to analyse the ranking of business environment of Western Balkan countries (Albania, Bosnia and Herzegovina, Croatia, North Macedonia, Montenegro, and Serbia). The aim of this paper is to analyse the relative positions of Western Balkan countries and to point out the differences or similarities among them and trends in past five years.

Analysis in this paper are based on survey data of international institutions: EBRD, World Bank, World Economic Forum, Heritage Foundation. By the analysis of indicators of competitiveness and quality of business we should point out competitive advantages and disadvantages of Western Balkan countries. According to the World Bank's report "Doing Business 2019", North Macedonia is the best ranked among the Western Balkan countries regarding conditions of doing business (10<sup>th</sup> rank), followed by Serbia (48<sup>th</sup>) and Montenegro (50<sup>th</sup>). The worse positions in the region is held by Bosnia and Herzegovina (89<sup>th</sup> rank).

According to the report of World Economic Forum for (Global Competitiveness Report for 2018), Serbia is the most competitive economy within the Western Balkan region (ranked in 65<sup>th</sup> place among 140 countries), followed by Croatia, Montenegro, Albania, North Macedonia. The worst ranked according to this report, is Bosnia and Herzegovina (ranked in 91<sup>st</sup> position). Serbia and Croatia are only countries from the region with the overall score above global median score (60). Serbia had the best improvement in overall score, compared to 2017.

According to the study of Heritage Foundation ("Index of economic freedom" 2019) North Macedonia is the best ranked country in Western Balkan region (ranked in 33<sup>rd</sup> position), and the only one country in the region with the score (71,1%) slightly above European average (68,6%). Albania is ranked in 52<sup>nd</sup> position, followed by Serbia on 69<sup>th</sup> position, which are also the countries with significant improvement comparing to last year. According to this report, Montenegro (ranked in 92<sup>nd</sup> position) is the worst ranked in region, with the lowest score in 2019 and highest declining of the score compared to 2018.

*Keywords:* business competitiveness, doing business, Western Balkan, investing intentions

## **1 Introduction**

In the last decades, the concept of competitiveness has attracted a lot of attention in academic society and in business practice. This concept has become a very important element of the success of every national economy. The core issues that are at the heart of the concept of national competitiveness relate to a better understanding of the ways in which it can improve the economic well-being and achieve a more equitable distribution of wealth (Krstić, Stanojević & Stanišić 2016).

The analysis of certain economies position in the region is important because if the positions of certain economies cannot be measured, they cannot be improved. The identification of the current economic situation in comparison with other competitors and its variation in the period are of crucial importance to policy makers, but also to the scientist sectors, for creating, updating, and implementing more efficient economic strategies and policies (Stošić & Minović 2014).

After two decades of implementation of intensive economic policies of the Western Balkan countries (WBC) have achieved macroeconomic stabilization but the results in reforming the economy, reforming the public sector and the public institutions are in insufficient level and continue to remain challenges for these countries in the future.

The main research objective of this paper is to analyse the ranking of business environment of Western Balkan countries (Albania, Bosnia and Herzegovina, Croatia, North Macedonia, Montenegro, and Serbia). The aim of this paper is to analyse the relative positions of WBC and to point out the differences or similarities among them.

Analysis in this paper are based on survey data of international institutions: World Bank, World Economic Forum and Heritage Foundation. By the analysis of indicators of competitiveness and quality of business we should point out competitive advantages and disadvantages of WBC.

According to the aim of this paper, after this introduction, the overview of literature and methodologies used in this paper are presented. In the next part of the paper, the evaluations of results of studies done by international institutions is given. As a final chapter, the conclusions of obtained results are made.

## **2 Literature review**

Great differences in the standard of living of certain countries are becoming a driving force of modern national economies' development, in terms of seeking the cause of those inequalities. Understanding the factors that drive the competitiveness has developed numerous theories and it has preoccupied creative curiosity of numerous academics (Krstić, Stanojević & Stanišić 2016).

At the national level, competitiveness is viewed as the ability of the country to increase the standard of living. Competitiveness can be defined as the set of institutions, policies, and factors that determine the level of productivity of a country.

The asymmetric development of West Balkan countries during the previous system and the low levels of economic growth in the first decade of the transition followed by increasing levels of unemployment, poverty, the large informal sector and fiscal evasion were the main obstacles in implementing deep institutional reforms and establishing a functional market economy in the Western Balkan's (Osmani 2015).

Another area where the West Balkan countries are lagging is in ensuring a level competitive playing field. Favouritism takes many forms. During the privatisation process, the rules were often designed to favour certain market players (typically, those with the best political connections). These large players

effectively divided the spoils of privatisation between themselves, leaving a substantial share of WB economies in dire straits. In Serbia, large retailers typically enjoy far higher margins than in the West. On a more positive note, Serbia is quite open to both investment and trade: the largest retail chain in Serbia is Belgian-owned, while the second largest is Croatian-owned. By contrast, the market in Croatia is generally more competitive than in Serbia. However, unofficially Croatia discourages Serbian-owned businesses from entering the Croatian market. Overall, however, investment and trade between WB countries is increasing, driven by the regional free trade (CEFTA) agreement brokered by the EU. While the EU is the leading trading partner of the WB nations, the region itself is the second most important export market for most of them. Nevertheless, far more needs to be done if a truly competitive regional market is to become a reality in the Western Balkans (EEAG 2016).

The concept of a state's competitiveness or the concept of international competitiveness is used in the analysis of economic performance of national economies. It compares countries by basic characteristics that determine the position in the international trade. These may be factors that are difficult to quantify, such as the capacity for technological innovation, degree of specialization of the product, the value of after-sales services and so on.

Acemoglu, Johnson and Robinson (Krešić, Milatović & Sanfey 2017) provide a theoretical framework on how differences in economic institutions the fundamental cause of differences in economic development are. As the authors put it, economic institutions are important because they influence the structure of economic incentives in society. For instance, aspects of an unfavourable business environment such as poor property rights and a biased judiciary remove the incentives for firms to invest or adopt more efficient technologies.

A part of the research related to issues of transitional changes and economic reforms was dedicated to the Western Balkans. The authors, mostly from this region have studied certain economic performances within the region, as well as the challenges in the process of accession to EU. As Stosic and Minovic (2014) are pointing out, significant existing progress achieved in most WBC still was not satisfactory. In order to fulfil the conditions for progress, to which all countries of the region strive, and provide the necessary intensive, long-term sustainable economic development and improve the competitiveness of business, it is necessary to implement several structural changes in the economic sphere.

Initiating, maintaining, and enhancing the economic growth requires decisive action of the creators of the development policies in order to improve the competitiveness of their countries and future economic prospects. Reforms and proper set of investments become crucial for economic transformation that leads to a sustained high economic growth over the long term. Therefore, it is imperative to increase competitiveness which should be at the top of the agenda of economic reforms in a country (Krstić, Stanojević & Stanišić 2016).

The most recent assessment of the Western Balkan countries available and published by the European Commission points to a low level of economic competitiveness: “Critical parts of the region’s economies are uncompetitive. None of the Western Balkans can currently be considered a functioning market economy nor to have the capacity to cope with the competitive pressure and market forces in the union (European Commission 2018).”

Although the EU reports on progress made by the Western Balkan countries towards accession include detailed information on the economic situation (including macroeconomic data) of each country, they are not intended to serve as a comparative tool. Obviously, for political and diplomatic reasons, the European Union is not in favour of creating a ranking of the “best” candidates (Kittova & Steinhauser 2018).

### 3 Methodology

There are a lot of different methodologies that have been formed and widely applied in the world, that are dealing with measuring competitiveness. In this study we decided to use models developed by international institutions:

- World Bank Group (“Doing business”),
- World Economic Forum (“Global Competitiveness Index”) and
- Heritage Foundation (“Index of Economic Freedom”).

The idea of these studies is to evaluate impartially and on continuous basis, jet largely based on strong subjective elements, some key performances of business environment competitiveness in different countries in the world or some regions. Therefore, an important analytical framework for identifying the relative positions of the economies and monitoring their progress, based on the so-called “soft data” has been created.

Analytical-empirical research method was used in the analysis of the competitiveness of business environment in WBC, which is supported by studying the adequate and varied literature, as well as opinions, statements and conclusions of the respective authors. During the theoretical and methodological research in the process of making this work following methods are been used:

- Historical - descriptive method,
- Analytical methods,
- Comparative methods and
- Empirical methods.

The competitiveness of an economy is measured through a *Global competitiveness index* (GCI). The GCI 4.0 introduces a new progress score ranging from 0 to 100. The frontier (100) corresponds to the goal post for each indicator and typically represents a policy target. Each country should aim to maximize its score on each indicator, and the score indicates its current progress against the frontier as well as its remaining distance. This approach emphasizes that competitiveness is not a not a zero-sum game between countries—it is achievable for all countries. There are a total of 98 indicators in the index, derived from a combination of data from international organizations as well as from the World Economic Forum’s Executive Opinion Survey. These are organized into 12 pillars in the GCI 4.0, reflecting the extent and complexity of the drivers of productivity and the competitiveness ecosystem. These are: Institutions; Infrastructure; ICT adoption; Macroeconomic stability; Health; Skills; Product market; Labour market; Financial system; Market size; Business dynamism; and Innovation capability (World Bank Group 2019).

Since its inception in 1995, the *Index of Economic Freedom* has provided powerful evidence that the empowerment of individuals within a system of open and competitive markets is the answer to that simple yet profoundly consequential question. As the Index has documented over the past 25 years, the most critical variable in sustaining the economic dynamism and wealth of nations is economic freedom, which is about dispersing economic power and decision-making throughout an economy and—most important—empowering individuals with greater opportunity and more choices. The Index findings over the past two-and-a-half decades have validated several important policy ramifications, including that (Miller, Kim & Roberts 2019):

- Private ownership and the protection of free enterprises by the rule of law encourage effort and initiative far more than is possible under collectivism and socialism.
- Governments that dominate their countries’ economies tend to impoverish their citizens through economic stagnation.
- Competition, facilitated by overall regulatory efficiency, promotes greater productivity and a more efficient allocation of resources than does central planning.

- Countries that have adopted and practiced open-market policies in the areas of trade, investment, and banking do better than those that are protectionist or that shun economic linkages with others.
- Implementing policies that address these four interwoven aspects effectively creates an entrepreneurial environment that is conducive to practical solutions to a wide range of economic and social challenges that are faced by most of the world's societies.

*Doing Business* measures regulations affecting 11 areas of the life of a business. Ten of these areas are included in this year's ranking on the ease of doing business: starting a business, dealing with construction permits, getting electricity, registering property, getting credit, protecting minority investors, paying taxes, trading across borders, enforcing contracts and resolving insolvency. *Doing Business* also measures labour market regulation, which is not included in this year's ranking (World Bank Group 2019).

## 4 Research

### 4.1 The Global Competitiveness Index

In order to estimate the effect of economic regulation on WBC's secondary data are used. Table 1 provides the ranking of WBCs according to the total number of countries.

Table 1: Global Competitiveness Index for 2018

Country	2017	2018	Rank among WBC in 2018	Score 2018
Serbia	70	65	1	60,9
Croatia	66	68	2	60,1
Montenegro	73	71	3	59,6
Albania	80	76	4	58,1
North Macedonia	n/a	84	5	56,6
Bosnia and Herzegovina	90	91	6	54,2

Adapted from World Bank Group (2018).

Since the global median score for 2018 is 60,0, according to the data from the Table 1, only Serbia and Croatia reached the global average, leaving all other WBC behind. Comparing to year 2017, Serbia is showing greatest progress in ranking, moving up for 5 ranks, while Croatia is deteriorating for 2 ranks. Although Serbia is best ranked among WBC, there are differences among components of overall rank, as presented in Table 2.

Table 2: Best ranking of WBC by components

Component	Best ranked in 2018 among WBC
Institutions	Montenegro
Infrastructure	Croatia
ICT adoption	Croatia
Macro-economic stability	Serbia
Health	Albania
Skills	Albania
Product market	Montenegro
Labour market	Montenegro

Financial System	Montenegro
Market size	Serbia
Business dynamism	Albania
Innovation capability	Serbia
<b>OVERALL</b>	<b>Serbia</b>

Table 3 shows the ranking in 2018, by components and comparing to average rank for each component.

Table 3: Ranking by components

Components	Albania	Bosnia and Herzegovina	Croatia	North Macedonia	Montenegro	Serbia	World Average
Institutions	68	111	74	85	63	76	80
Infrastructure	100	89	36	80	86	48	73
ICT adoption	74	86	53	70	58	60	67
Macro-economic stability	97	73	106	70	102	64	85
Health	45	52	51	71	55	67	57
Skills	47	87	65	81	52	56	65
Product market	58	106	71	107	45	66	76
Labour market	34	112	96	78	25	52	66
Financial System	105	83	62	80	51	79	77
Market size	108	99	78	109	132	75	100
Business dynamism	48	106	81	57	50	59	67
Innovation capability	91	114	63	98	74	56	83
<b>OVERALL</b>	<b>76</b>	<b>91</b>	<b>68</b>	<b>84</b>	<b>71</b>	<b>65</b>	<b>76</b>

As the Table 3 shows, the worst ranks in the region has Bosnia and Herzegovina, especially in fields of institutions, labour market and innovation capability. Ten among twelve components of the overall rank are below worlds average, with only macro-economic stability and health being above that average. On the other hand, Serbia's all components of the rank are above global average, except health and financial system. Albanian's outstanding components that are below global average rang are Infrastructure and Financial System. Surprisingly, Croatia's worst ranks are for components macro-economic stability, labour market and business dynamism. As in case of Bosnia and Herzegovina, North Macedonia's components are mostly below world average, especially health, skills, product market, labour market and innovation capability. On the other hand, Montenegro has only three, among twelve components, that are below world average: market size, infrastructure and macro-economic stability.

#### 4.2 The Ease of Doing Business Index

Doing Business recognizes that the state plays a fundamental role in private sector development. Governments support economic activity by establishing and enforcing rules that clarify property rights and reduce the cost of resolving disputes, increase the predictability of economic interactions and provide contractual partners with core protections against abuse. Table 4 shows the rank among WBC in 2018.



Table 4: Ease of Doing Business Index in WBC in 2018

Country	Rank	Score	Rank among WBC in 2018
North Macedonia	10	81,55	1
Serbia	48	73,49	2
Montenegro	50	72,73	3
Croatia	58	71,40	4
Albania	63	69,51	5
Bosnia and Herzegovina	89	63,82	6

Adapted from World Bank Group (2019)

As we can see from the Table 4, North Macedonia is the best ranked among the WBC regarding conditions of doing business (10<sup>th</sup> rank), followed by Serbia (48<sup>th</sup>) and Montenegro (50<sup>th</sup>). The worse positions in the region is held by Bosnia and Herzegovina (89<sup>th</sup> rank). Table 5 indicates scores by the individual topics, with average score by topics and its standard deviation.

Table 5: Scores by the individual topic

Score on Topics	SRB	MNE	MKD	HRV	BIH	ALB	Average	Standard deviation
Starting a Business	92,59	86,65	92,08	82,62	59,57	91,58	84,18	12,67
Dealing with Construction Permits	84,42	70,88	83,38	55,70	53,22	57,01	67,44	14,16
Getting Electricity	70,01	59,19	81,43	80,50	60,26	57,71	68,18	10,81
Registering Property	72,60	65,78	74,50	74,07	61,99	62,08	68,50	5,91
Getting Credit	65,00	85,00	85,00	55,00	65,00	70,00	70,83	12,01
Protecting Minority Investors	56,67	61,67	80,00	66,67	58,33	71,67	65,84	8,87
Paying Taxes	74,75	76,67	84,72	72,68	60,43	64,91	72,36	8,66
Trading across Borders	96,64	88,75	93,87	100,00	91,87	96,29	94,57	3,96
Enforcing Contracts	61,41	66,75	67,79	70,60	59,67	56,44	63,78	5,44
Resolving Insolvency	60,78	65,99	72,69	56,20	67,83	67,42	65,15	5,82
Average	<b>73,49</b>	<b>72,73</b>	<b>81,55</b>	<b>71,40</b>	<b>63,82</b>	<b>69,51</b>	<b>72,08</b>	
Standard deviation	13,73	10,83	8,22	14,16	10,59	13,97		
Total rank among WBC	2	3	1	4	6	5		

Legend: SRB – Serbia, MNE – Montenegro, MKD – North Macedonia, HRV – Croatia, BIH – Bosnia and Herzegovina, ALB – Albania.

From the Table 5, we can conclude that:

- All countries have above average scores in Trading across Borders.
- All countries except Bosnia and Herzegovina have above average scores in Starting business.
- All countries except Bosnia and Herzegovina and Albania have above average scores in Paying Taxes.
- Enforcing Contracts and Resolving Insolvency are topics with lowest average scores in the West Balkan region.
- Individually observed, lowest scores have Bosnia and Herzegovina for Dealing with Construction Permits, and Croatia for that same topic and for Getting Credit.
- Highest standard deviation on individual topic has “Dealing with Construction Permits” with results spread from lowest 53,22 (Bosnia and Herzegovina) to highest 84,42 (Serbia). Next

highest standard deviation on individual topics goes to “Starting a Business”, from lowest 59,57 (Bosnia and Herzegovina) to highest 92,59 (Serbia).

- Lowest standard deviation on individual topic has “Trading across Borders” which indicates and confirms that the topic is most balanced among WBC.
- From the analyse of standard deviation of scores for individual topic in the range of individual country, the most volatile results have Croatia and the least volatile results has North Macedonia. Croatian scores vary from 55,00 (Getting Credit) to 100,00 (Trading across Borders), while North-Macedonian scores are more even and vary from 67,79 (Enforcing Contracts) to 93,87 (Trading across Borders).

The quality of business environment in Bosnia and Herzegovina remains highly problematic and the country continues to lag other economies in WBCs, reflecting the deep-rooted problems in the country. Its performance is particularly weak for the indicators such as dealing with construction permits and protecting minority investment (World Bank Group 2019).

Although North Macedonia has highest average score, its lowest scores among all topics are enforcing contracts and resolving insolvency.

#### 4. 3 Index of Economic Freedom

The 2019 Index global average economic freedom score is 60.8, the third-highest level in the Index’s 25-year history. Of the 180 economies ranked, six are considered free, and an additional 88 are considered to be at least moderately free. At the other end of the spectrum, 86 economies received scores below 60 and are judged mostly unfree or repressed. The slight decline in global economic freedom in 2019 was driven by in-cresed protectionism in some major markets, setbacks in judicial effectiveness, and attempts by governments to influence business and consumer decision-making through regulation and government spending (Miller, Kim i Roberts 2019).

According to the study of Heritage Foundation (“Index of economic freedom” 2019) North Macedonia is the best ranked country in Western Balkan region (ranked in 33rd position), and the only one country in the region with the score (71,1%) slightly above European average (68,6%). Albania is ranked in 52<sup>nd</sup> position, followed by Serbia on 69<sup>th</sup> position, which are also the countries with significant improvement comparing to last year. According to this report, Montenegro (ranked in 92<sup>nd</sup> position) is the worst ranked in region, with the lowest score in 2019 and highest declining of the score compared to 2018. Results are presented in Table 6.

Table 6: Index of Economic Freedom in WBC in 2019

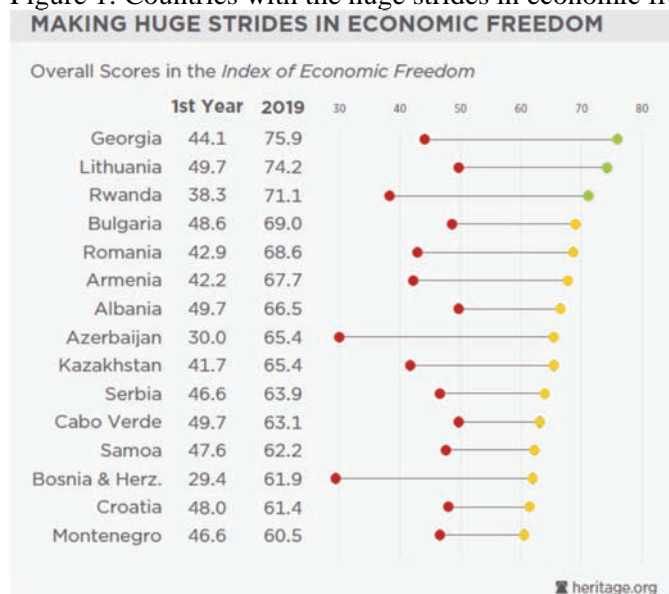
Country	2014	2015	2016	2017	2018	2019	<i>Index 19/18</i>	<b>Rank 2019</b>	<b>Rank among WBC</b>
North Macedonia	68,60	67,10	67,50	70,70	71,30	71,10	<i>100</i>	33	1
Albania	66,90	65,70	65,90	64,40	64,50	66,50	<i>103</i>	52	2
Serbia	59,40	60,00	62,10	58,90	62,50	63,90	<i>102</i>	69	3
Bosnia and Herzegovina	58,40	59,00	58,60	60,20	61,40	61,90	<i>101</i>	83	4
Croatia	60,40	61,50	59,10	59,40	61,00	61,40	<i>101</i>	86	5
Montenegro	63,60	64,70	64,90	62,00	64,30	60,50	<i>94</i>	92	6
<b>EUROPE</b>	<b>67,10</b>	<b>67,00</b>	<b>66,90</b>	<b>68,00</b>	<b>68,80</b>	<b>68,60</b>	<i>100</i>		



As shown in Table 6, all countries are in zone of moderately free, except of North Macedonia which passed into mostly free economic environment from 2017. The global average economic freedom score in the 2019 Index is 60,8, a 0,3-point setback from last year but still the third-highest level in the 25-year history of the Index. Six (Hong Kong, Singapore, New Zealand, Switzerland, Australia, and Ireland) earned the designation of “free” with scores above 80. All countries, except Montenegro have economic freedom score above global average.

Miller, Kim and Roberts (2019) are pointing out countries with the huge strides in economic freedom from the first year index was calculated until 2019 for all WBC, as shown in Figure 1. Nevertheless, they still emphasize that Montenegro experienced sharp declines in economic freedom, with a failure to move forward with privatization of state-owned enterprises.

Figure 1: Countries with the huge strides in economic freedom



Source: Miller, Kim & Roberts (2019, 15)

## 5 Conclusion

The main research objective of this paper is to analyse the ranking of business environment of Western Balkan countries (Albania, Bosnia and Herzegovina, Croatia, North Macedonia, Montenegro, and Serbia). The aim of this paper is to analyse the relative positions of WBC and to point out the differences or similarities among them.

Competitiveness has become the dominant economic theme. Its character, in addition to the traditional supply needs to be more competitive or better than others, contributed to the world economic crisis through which passes all the economy. The importance of competitiveness stems from the fact that it finds its use of all available resources. For each country, it is important to look at the quality of the use of available resources. Economic competitiveness of the Western Balkan countries is uneven. Concept of competitiveness of the country is a source of important information enabling investors to perceive potentials of their future investment returns. Poor ranking of a country signals to potential investors to take additional measures of caution about their investing intentions. Beyond that, the level of competitiveness of an economy has a material role in its economic growth and development.

On the basis of the Global Competitiveness Index, Ease of Doing Business Index and the Index of Economic Freedom values of the Western Balkan countries, it is possible to compare the performance

of the WBC and create a ranking where value 1 represents the country with the best index results within the region, as shown in table 7.

Table 7: Comparison of WBC

	North Macedonia	Albania	Serbia	Bosnia and Herzegovina	Croatia	Montenegro
Global Competitiveness Index	5	4	1	6	2	3
Ease of Doing Business Index	1	5	2	6	4	3
Index of Economic Freedom	1	2	3	4	5	6
<b>Average position in the region</b>	<b>2,33</b>	<b>3,67</b>	<b>2,00</b>	<b>5,33</b>	<b>3,67</b>	<b>4,00</b>

According to our findings and based on average position by all three indexes in the WB region, the best overall economic position among the Western Balkan countries belongs to Serbia, followed by North Macedonia. On the other hand, country assessed as the worst in the region is Bosnia and Herzegovina.

In most WBC infrastructure needs to be upgraded significantly. If the financial system is to truly support the creation of a competitive regional economy, far more needs to be done. The region's current bank-orientated system leaves little room for innovative start-ups to be financed. The creation of regional financial markets (they currently only exist in a rudimentary form, except to a certain extent, in Croatia), regional venture funds, angel investor firms and non-deposit financial institutions would be very useful in tapping into the productive potential of the WB population.

Cooperation between WBC needs to go beyond just free trade and investments. For example, Serbia is quite open to both investment and trade. By contrast, the market in Croatia is generally more competitive than in Serbia, although Croatia discourages Serbian-owned businesses from entering the Croatian market. Overall, however, investment and trade between WBC is increasing, driven by the regional free trade (CEFTA) agreement brokered by the EU. While the EU is the leading trading partner of the WB nations, the region itself is the second most important export market for most of them. Nevertheless, far more needs to be done if a truly competitive regional market is to become a reality for the Western Balkans Countries.

Further research is required to examine barriers in more detail, for example access to financing, tax rates, restrictive labour regulations, capacity to innovate, supply of infrastructure, educated workforce, work ethic in national labour force, etc.

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