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## THE ANALYSIS OF FINANCIAL AND NON-FINANCIAL SUPPORT TO THE SECTOR OF SMALL AND MEDIUM ENTERPRISES IN THE REPUBLIC OF SRPSKA

### АНАЛИЗА ФИНАНСИЈСКЕ И НЕФИНАНСИЈСКЕ ПОДРШКЕ СЕКТОРУ МАЛИХ И СРЕДЊИХ ПРЕДУЗЕЋА У РЕПУБЛИЦИ СРПСКОЈ

**Summary:** *The aim of this paper is to analyze the role and importance of financial and non-financial instruments of supporting the sector of small and medium enterprises (SMEs) in the Republic of Srpska (RS). For that purpose, in late 2013 and early 2014, there was conducted a quantitative research on a sample of 110 respondents on the whole territory of RS, with the aim of finding the answers to the following question: What is the reason that a large number of SMEs in RS fail to provide adequate financial and non-financial support to their business activity and what measures should be taken in order to improve the current situation? In order to specify the research problem, we ask ourselves if the existing instruments of financial and non-financial support to the sector of SMEs in the RS are sufficiently developed and accessible, as to contribute to the successful growth and development of the said enterprises? We found that the above mentioned instruments of support to the SME sector in RS are not sufficiently developed. Respondents were acquainted with the sole instruments and models of financial and non-financial support that exist in RS. According to the results of the empirical research, we conclude that creating and mastering the models and instruments of financial and non-financial support to SME sector in the RS and providing the adequate business climate for their successful functioning, will increase the availability of favourable financial means for SMEs, as well as the possibility of using the positive aspects of clusters, guarantee funds, factorings and other forms of entrepreneurship infrastructure.*

**Key words:** *Small and medium enterprises (SMEs), instruments and models of financial and non-financial support.*

**Jel classification:** G23

**Резиме:** *Циљ овог рада је анализа улоге и значаја инструмената финансијске и нефинансијске (ФиН) подршке сектору малих и средњих предузећа (МСП) у Републици Српској (РС). У ту сврху, крајем 2013. године и почетком 2014. године, проведено је квантитативно истраживање на узорку од 110 испитаника на цијелој територији РС, са циљем добијања одговора на питање: због чега велики број МСП у РС не успијева да обезбједи адекватну ФиН подршку свом пословању и које мјере је потребно предузети у циљу унапрјеђења постојећег стања, односно, да ли су постојећи инструменти ФиН подршке сектору МСП у РС довољно развијени и приступачни да би допринијели успјешном расту и развоју МСП? Установили смо да наведени инструменти подршке сектору МСП у РС нису довољно развијени. Испитаници су упознати са начином рада искључиво инструмената и модела ФиН подршке који постоје у РС. Сходно резултатима емпиријског истраживања, закључујемо да би креирање и усавршавање модела и инструмената ФиН подршке сектору МСП у РС и обезбјеђивање адекватне пословне климе за њихово успјешно функционисање повећало доступност повољних финансијских средстава за МСП, као и могућност кориштења позитивних аспеката кластера, гарантних фондова, факторинга и других облика предузетничке инфраструктуре.*

**Кључне ријечи:** *мала и средња предузећа, инструменти и модели финансијске и нефинансијске подршке.*

**JEL класификација:** G23

## 1. INTRODUCTION

Small and medium enterprises (SMEs) have an important role in the economic structures of successful economies in the world. They dominantly participate in the total number of enterprises in the non-financial business sector, generate employment and contribute to gross domestic product (GDP) growth and growth of exports (OECD 2013).

The importance of the SME sector is being recognized in the world and in our country. The relevant institutions are making efforts to create a favorable business environment and legal prerequisites for making new SMEs and for the development of existing ones. In order to improve the regulation of this area, in July 2013, the new „Law on SME Development“ was adopted in the Republic of Srpska<sup>1</sup> (RS) (Official Gazette of RS 2013), which replaced the former „Law on Supporting SME Development“ (Official Gazette of RS 2009).

Competent institutions in developed economies in the world stimulate growth and development of SMEs and entrepreneurship (Vukmirović 2012). For that cause, many instruments and models of financial and non-financial<sup>2</sup> (FaN) support to the SME sector are being developed (Petković and Berberović 2013). The achieved level of models and instruments application is various by countries. It may be a reason that there is a different level of development of SME sector in the world economies. Yet, there is inadequate number of FaN support to the SME sector in the RS.

*„...we have no ministry that deals exclusively with small and medium enterprises and entrepreneurs, we have no angel investors, venture capital funds, factoring companies or technology parks. Other instruments and institutions of entrepreneurial infrastructure (innovation centers, business districts, guarantee fund (author's note)) we do have, but they are generally underdeveloped and unevenly distributed throughout the territory of the Republic of Srpska“* (Official Gazette of RS 2013).

We define the research problem in this paper, using the following question: what is the reason that a large number of SMEs in RS fail to provide adequate FaN support to their business activity and what measures should be taken in order to improve the current situation? In order to specify the research problem, we ask ourselves if the existing instruments of FaN support to the sector of SMEs in the RS are sufficiently developed and accessible, as to contribute to the successful growth and development of the said companies?

The subject of the research in this paper is the theoretical and empirical analysis of FaN support to the SME sector in RS. We position the subject of the research in the field of theoretical economics and entrepreneurial economy. At the same time, other scientific disciplines and tighter economic areas will be treated as constants. The research area is geographically focused on RS, as a specific economic area. We explored the role, impact and importance of individual instruments of FaN support to the SME sector in RS, emphasising sources of financing of SMEs and level of owners and managers knowledge on forms of entrepreneurship infrastructure.

We have used structured questionnaire<sup>3</sup> (online polls), as a method of data collection, using representative sample on the entire territory of RS.

Discovering and understanding factors of institutional and non-institutional support to the SME sector in RS, are the main goals of this paper. Scientific contributions will be realized through scientific description, explanation, classification and prediction. Underdeveloped FaN instruments of supporting SMEs represent a major obstacle to progress and the positive prospects of the economy. Rise of awareness of stakeholders on the necessity of solving this problem represents social contribution of the paper. The research results presented in this paper can produce direct and/or indirect benefits to SME owners, the institutions that legally regulate this area, for the academic community and the whole public of the RS.

According to objectives of the research, the possibility of adequate FaN support to SME sector in RS will be treated as the dependent variable. The functioning of financial and non-financial

<sup>1</sup> Republic of Srpska is a state-building entity within Bosnia and Herzegovina. The research conducted in this paper will refer to this entity (author's note).

<sup>2</sup> Instead of financial and non-financial support, we will use abbreviation „FaN“ (author's note).

<sup>3</sup> The research was conducted during the preparation of the master thesis of the author of this paper (author's note).

institutions of supporting business environment for the growth and development of SMEs and entrepreneurship in the RS will be treated as an independent variable.

According to the previous, we define the basic hypothesis of this study as follows:

H0: By creating and mastering the models and instruments of FaN support to SME sector in the RS and providing the adequate business climate for their successful functioning, we will increase the availability of favourable financial means for SME, as well as the possibility of using the positive aspects of clusters, guarantee funds, factorings and other forms of entrepreneurship infrastructure.

In order to determine the significant elements of FaN support to the SME sector, we will approach the collection, processing and analysis of secondary and primary data. We used a quantitative online questionnaire as a data collection technique. We have sent emails to random electronic addresses of SMEs that we chose from APIF<sup>4</sup>'s database. During the analysis of the empirical data, we used the following methods: induction and deduction, historical and graphical method, methods of analysis and synthesis, analogies, similes, classification and compilation.

First, we will explore theoretical views on the subject of research, and then, we will determine the specific parameters and correlations between observed variables, using collected research results.

## 2. INSTRUMENTS AND MODELS OF FINANCIAL SUPPORT TO SME SECTOR

The largest problem of a small enterprise in the beginning of its business is finance. Regardless of the quality of an entrepreneur's idea, its realization would not be possible without the initial, start-up capital. An entrepreneur is not usually able to cover all of the enterprise financial needs from his own private incomes (savings, financial support from family or friends, etc.) In those situations, he tries to get the necessary capital from SME finance support instruments.

When it comes to providing external sources of finance, most of enterprises choose a loan from a commercial bank. Beside the standard loans from banks, microcredit organizations have an important role in lending to SMEs (Erić et al. 2012)

Microcredit organizations played an important role in financing start-up enterprises, mostly the independent ones. This was especially the case in the postwar growth of the Republic of Srpska and Bosnia and Herzegovina (Petković and Berberović 2013, 97).

However, our opinion is that resources from microcredit organizations should be the last choice for financing SMEs. The reason is their amazingly high interest rates.

Beside loans, enterprises usually choose the following forms of financial support:

- Leasing (operating<sup>5</sup> and financial<sup>6</sup>); Mikerević (2011) thinks that leasing contract needs to include the training of the leasing users, the transfer of knowledge and experience related to the equipment usage as well as the service, maintenance and replacement of some old parts of the equipment.
- Factoring, in its basic sense, adds up to a sale of an enterprise's short-term receivables immediately after invoicing factoring firms (Mikerević 2011). The income of a factoring firm is the commission charged from a seller. The commission span comes in a very few percent (2-3%) and up to 20% in some less developed countries.
- Venture capital funds provide resources for investing in new or high-risk enterprises. This is usually done in exchange for an ownership stake. Beside the financial support to SMEs, venture capital funds usually give professional support, too (Ćudić 2012).
- Mezzanine finance represents the bridge between two main forms of finance: the main debt and the capital. Although the use of mezzanine finance instruments has recently expanded, they are still used less compared to normal loan financing (Glavantis 2007, cited in Petković and Berberović 2013).
- Stock exchange markets.

<sup>4</sup> APIF – Agency for IT and financial services, <http://www.apif.net/>

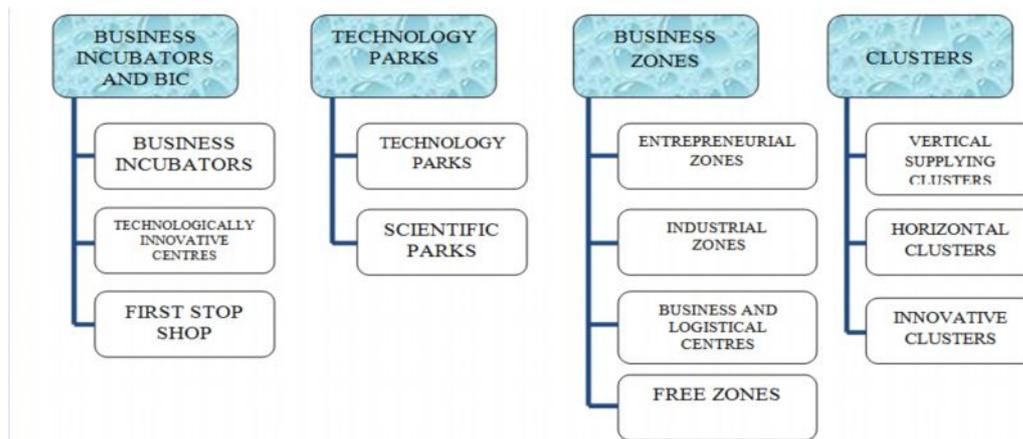
<sup>5</sup> "Business (operating) lease is short-term contract or a contract which could be terminated by unilateral announcement" (Mikerević 2011, 269).

<sup>6</sup> Unlike the operating leasing, financial leasing means shifting all risks and benefits from the leasing giver on the leasing recipient (Petković and Berberović 2013, 98)

### 3. INSTRUMENTS AND MODELS OF NON-FINANCIAL SUPPORT TO SME SECTOR

The existence of an adequate financial support to SME sector is necessary but insufficient for their successful business. The entrepreneur's infrastructure plays very important role in providing successful start of business and its future development. Forms of entrepreneurial infrastructure are shown in the picture 1.

Picture 1: Models of entrepreneurial infrastructure



Source: RS Government 2011, 30

Enabling finance to SMEs is more complicated than providing finance to a big enterprise. In the South-East Europe, 23.9% of small enterprises marked the access to finance as the main obstacle for their growth – compared with 18.2% of big enterprises (OECD n.d.)

Which are the main characteristics of non-financial instrument support to SME sector?

- Loan-guarantee funds (public guarantee schemes, corporative funds, international funds and mutual guarantee associations (Green, cited in OECD n.d.) have an important role in providing bank loans for SMEs. Taking the Guarantee Fund of The Republic of Srpska as an example, it is clear that loan guarantee funds give guarantees to business banks. These banks serve as an additional loan protection of clients whose projects are marked as a high-quality and perspective ones. The income of these funds is the premium for risk charged from a client.
- Business incubators (state incubators, corporation incubators, franchise incubators and university-business incubators (Vukmirović 2012) are very important elements of the entrepreneurial infrastructure. There are about 4.000 incubators in the world. About 1.000 of them are located in South America and the European Union. The result of running European incubators is the creation of 40.000 new jobs every year. Enterprises which go through the incubator have a bigger chance to continue existing than other SMEs (Vasilescu 2008).
- Clusters<sup>7</sup> have a very important role in the world economies. It is a fact that globalization has strengthened the role of clusters. The rapid globalization is the reason why resources move to more attractive regions, which led to a redefinition of the cluster role. There are about 2000 statistically important clusters in Europe. They are defined as regional agglomerates. About 38% of workforce in Europe is employed in companies which are members of clusters (Commission of European Communities 2008a, 3).
- Technological (scientific, research, explorer) parks are founded with the aim of giving support to new SMEs. These technological parks are usually connected with high technologies and knowledge-based enterprises. In accordance with their organization, they offer different services to enterprises that they want to attract.

<sup>7</sup> The word cluster comes from the English language and means "a bunch" or "a set" of similar or complementary small enterprises gathered around shared services for business transactions, distribution, export, marketing etc. (Vukmirović 2006, 371).

- Public-private partnerships occur because of the risk of division between a private partner and public administration. The risk could be the result of project characteristics, political circumstances, public pressure etc. It is manifested in two forms: simple contract partnership, where the private sector is involved in designing and financing, and institutional public-private partnership where there is a legal entity in a joint partner ownership (Commission of European Communities 2008b).

### 3. FINANCIAL AND NON-FINANCIAL SUPPORT TO THE SME SECTOR IN RS

SMEs play very significant role in the economy of RS. It can clearly be seen in the „Annual report for SMEs for 2011“<sup>8</sup> (RS Government 2012)

There were 14.935 active enterprises at the end of 2011 operating in the Republic of Srpska, with 14.871 enterprises belonging to the category of SMEs. Micro-enterprises with up to 9 employees are dominant in the structure of enterprises in RS, and they make up 85.69% of the total number of enterprises. Small enterprises make up 11.27% of the total number of enterprises, and medium sized enterprises represent 2.61%. There is 0.43% of large enterprises in RS.

The importance of the SME sector is being recognized, so the relevant institutions in RS are making an effort to create a favorable business environment and legal prerequisites for establishing new SMEs and for the development of existing ones (Jevtić 2004).

#### 3.1. Financial Support to the SME Sector in the Republic of Srpska

Financial support to SME sector in RS is based on grants and credit lines. Grants are provided by the RS Government and partly by IRB RS (RS Government 2011). Credit lines are provided by IRB RS, banks and microcredit foundations. In addition, a certain role in providing direct and indirect financial support to SMEs is played by some international projects and donors (Ibid 2011).

Within the portfolio of loans provided by IRB RS, there are several credit lines relating to SMEs and entrepreneurs.

*Table 1. Loans of the Republic of Srpska Investment-Development Bank to SMEs and entrepreneurs*

	Type of loans of The Republic of Srpska Investment-Development Bank (IRBRS)	Number of loans	Total value (BAM)	Average value of loan (BAM)
1	Loans for start-up activities	101	3.546.287	35.112
2	Loans for microbusiness in agriculture	1.867	34.386.154	18.418
3	Loans for agriculture	108	79.868.362	739.522
4	Loans for entrepreneurs and enterprises	701	501.046.115	714.759
5	Loans for small and medium enterprises – EAF Project	112	68.581.230	612.332
6	Loans for small and medium enterprises - EIB	20	97.783.437	4.889.172
7	Loans for enterprises	28	40.561.049	1.448.609
8	Loans for agriculture and agricultural processing	20	41.924.750	2.096.238
	<b>TOTAL</b>	<b>2.957</b>	<b>867.697.384</b>	<b>293.438</b>

Source: Author, adjusted from official site of IRB RS

There are BAM 1.5 million planned for subsidies for the development of the manufacturing industry in the 2015 Budget of the Ministry of Industry, Energy and Mining of RS (Official Gazette of RS 2014). In addition, BAM 50.000 are planned for the implementation of „The strategy for development of SMEs, entrepreneurship and the establishing of business zones“ and BAM 15.000 as a grant for the liquidation proceedings.

<sup>8</sup> The main deficiency in the analysis, which is highlighted in the report, is that RS institutions for statistical monitoring of SMEs data are not yet developed on the basis of EU methodology according to EUROSTAT (Petković i Berberović 2013, 26).

In May 2014, the fifth Balkan Investment Forum was held in RS. The Forum was organized and financed within the project „VIBE<sup>9</sup>“ (Republic Agency for SME Development 2013a). This was a unique opportunity for entrepreneurs from RS, and for the ones that have an ambition to become entrepreneurs, to find out more about new methods and models of investment. Organizing similar events can contribute to an affirmative representation of the role of venture capital in the financing of SMEs.

Banja Luka stock exchange can provide finance for SMEs, but that instrument of financing is still unused in RS. It seems that owners of SMEs in RS are not willing to share ownership with others, or to introduce professional management, which is necessary for SMEs to grow beside market borders of RS. „Only one joint-stock company is listed on the Banja Luka Stock Exchange upon the completion of the initial public offering (IPO) (Republic Agency for SME Development 2013b).

### 3.2. Non-Financial Support to SME Sector in the Republic of Srpska

Within the fulfillment of the objectives of the "European Charter for Small Enterprise" and adopted laws and policies at the level of the Government of the Republic of Srpska, the following support to SMEs in RS exist and operate: Council for SMEs and Entrepreneurship Development and the Department for SME's and Entrepreneurship Development in the Ministry of Industry, Energy and Mining. The Republic Agency for SME Development is a coordinating body of the Government in the implementation of adopted strategies and policies.

The development network for supporting SMEs, apart from those already mentioned, is provided by municipal departments for economy, local development agencies, chambers and unincorporated commerce, scientific research institutions, educational institutions, various trade associations, media and other parties interested in the development in this field, IRB RS and Guarantee Fund of RS (RS Government 2011).

One of the forms of non-financial assistance to the SME sector is enabling enterprises to achieve specific contacts, the exchange of ideas, goods and services with enterprises from other countries. For this purpose, after consulting institutions of RS Government, the Republic Agency for SME Development, has launched some activities related to establishing the European Network of Entrepreneurship of the Republic of Srpska during 2012. The aim of this activity is achieving membership in the Enterprise Europe Network<sup>10</sup>, which was established in 2008 by the European Commission. The benefits to be gained by enrolling in this network are: strengthening the competitiveness of SMEs, better access to information and improved access to markets and transnational economies, encouraging innovation and building innovative capacity (Republic Agency for SME Development 2013c).

A significant advantage in business can be realized by enterprises which have the opportunity to join the cluster. Therefore, there are multiplied activities related to clustering in the RS in recent years, a larger number of clusters are being made and more enterprises are recognizing the benefits of clustering. Clustering is supported by both the Government of the Republic of Srpska, and IRB RS.

In addition to this kind of support, the establishment of clusters is also supported by local development agencies, as is the case in Banja Luka and Srbac. The largest number of clusters and launched cluster initiatives are concentrated in the wood processing and furniture production, metal and electrical industry, textile, leather and footwear and food industry (RS Government 2012b).

## 4. EMPIRICAL RESULTS OF THE RESEARCH

For the purpose of the paper we conducted a quantitative research using an online poll, a printed poll and a poll in the form of a word document, using the random sampling method. Some questions were closed, some were multiple-choice questions, and some were open and they targeted

<sup>9</sup> VIBE - Venture Initiative in the Balkan Europe. This project is focused on developing innovative and entrepreneurial systems throughout Southeast Europe. Its aim is to encourage private investment in innovative SMEs in partnership with public initiatives and investments (Republic Agency for SME Development 2013b).

<sup>10</sup> Enterprise Europe Network consists of more than 600 partner organizations and institutions that engage more than 4.000 experts in the field of entrepreneurship, innovation and technology transfer, with the aim of promoting enterprises on a local and European level (Republic Agency for SME Development 2013b).

respondents' opinions. The research was conducted in the period between December 12<sup>th</sup>, 2013 and December 31<sup>st</sup>, 2013. During that period, 62 polls were completed, while the rest of them were completed during the period between January 20<sup>th</sup>, 2014 and March 14, 2014. The research was conducted in 5 cities and 14 municipalities in the Republic of Srpska.<sup>11</sup> Respondents who are owners or managers of SMEs (enterprises with less than 250 employees) completed the poll individually. The number of collected polls is relatively small compared to the statistical weight (0,74 % compared to the total number of enterprises<sup>12</sup> in 2011), but because of the manner of sample selection, that fact does not diminish the representativeness of the chosen sample.

#### 4.1. Limitations of the Research

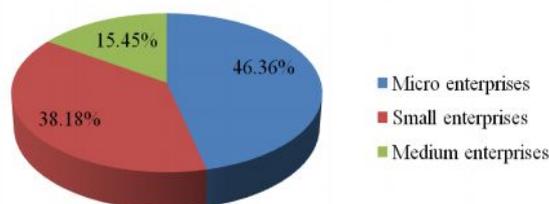
There were a few limitations that slowed down the pace of conducting the research and decreased the total number of collected polls:

- A great number of owners and managers were not interested in completing the poll, which shows that they are inconsiderate in relation to academic research;
- The possibility that respondents' answers were subjective and that they imposed some personal opinions;
- The latest analysis of SME sector in the Republic of Srpska refers to 2011, which means that some indicators may be outdated to a certain degree;
- A great number of sent emails did not reach their final destination because the database was not up to date. That is why an initiative should be launched that would form a singular APIF's database of SMEs in the Republic of Srpska formed specifically for research purposes.

#### 4.2. General Information about Enterprises from the Sample

The average period for which these enterprises have been existing is 13,88 years, which means that an average enterprise participating in the sample was established in 2000. Still, this information cannot be considered completely relevant because the standard deviation is high<sup>13</sup> (9.93). In order to acquire more relevant information, mode and median will be used as a measure of central tendency. The median is represented by 2011. That means that 50% of the enterprises were established before 2011, and the other 50% were established after 2011. Most of the enterprises (10 or 9.1%) in the sample were established in 2007<sup>14</sup>. According to their size, the enterprises in the sample are divided in the following manner:

*Fig 1: SMEs in the sample classified by size*



Source: Author

When it comes to the legal form of the enterprises in the sample, the following can be noticed:

<sup>11</sup> The geographic structure of collected polls: Banja Luka (51), Trebinje (6), Sipovo (3), Gradiska (4), Laktasi (6), Vlasenica (1), Mrkonjic Grad (3), Knezevo (10), Prijedor (3), Doboj (6), Prnjavor (2), Ribnik (2), Istocno Sarajevo (2), Zvornik (2), Vukosavlje (1), Srbac (3), Bijeljina (3) and Teslic (1).

<sup>12</sup> According to the data from the annual report on SMEs and craft and entrepreneurial activity in the Republic of Srpska, the number of SMEs in 2011 was 14.871 (RS Government 2012).

<sup>13</sup> Standard deviation shows how many elements of a set deviate from the arithmetic mean of the set (author's note).

<sup>14</sup> Mode is a measure that is very often used in descriptive statistics and it represents the value that appears most frequently in the sample (author's note).

Table 2: The legal form of the SMEs from the sample

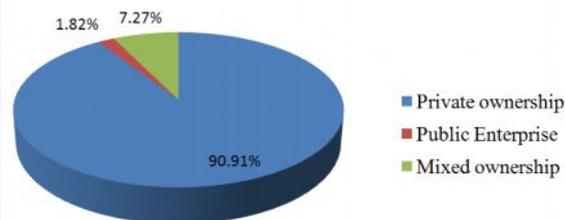
The legal form of the SMEs from the sample	Number of SMEs	Participation in the total sample
Public Limited Company - PLC	11	10.00%
Limited Liability Company – LTD	85	77.27%
Cooperative	3	2.73%
Independent business enterprise - IBE	10	9.09%
Other	1	0.91%
<b>TOTAL</b>	<b>110</b>	<b>100.00%</b>

Source: Author

Out of 85 LTDs, 38 enterprises (44.70%) are in the category of micro enterprises, 37 (43.53%) are in the category of small enterprises, while the remaining 10 enterprises (11.76%) are in the category of medium enterprises. Out of 10 enterprises that are in the category of independent business enterprises, seven are micro enterprises, while three of them are small enterprises. It is assumed that, as a rule, PLCs have more employees. In this sample, seven enterprises out of 11 PLCs are medium enterprises, while two are small and two are micro enterprises.

Below is represented the ownership structure of SMEs in the sample:

Fig 2: The ownership structure of SMEs in the sample



Source: Author

When it comes to the number of employees in the SMEs in the sample, the data are represented in the table below:

Table 3: Statistical data about employees in the sample SMEs

STATISTICS	WHOLE SAMPLE	LEGAL FORM OF SMEs			THE OWNERSHIP STRUCTURE OF SMEs	
		Public Limited Company	Limited Liability Company	Independent Business Enterprise	Private ownership	Mixed ownership
Average number of employees	29.00	75.27	26.85	5.60	23.38	86.00
Standard deviation	42.80	55.18	40.38	5.34	38.41	37.53
Mode	2.00	#N/A <sup>15</sup>	2.00	2.00	2.00	#N/A
Median	10.00	70.00	11.00	3.00	9.50	70.50

Source: Author

Because the standard deviation is very high, more attention needs to be dedicated to the analysis of the mode and median. Most of the enterprises (15 of them) have 2 employees. It is interesting that the median of private enterprises is 9.5, i.e. 50% of them are micro enterprises, while 50% are SMEs, which to a larger degree matches the median of the main sample. It is clear that most

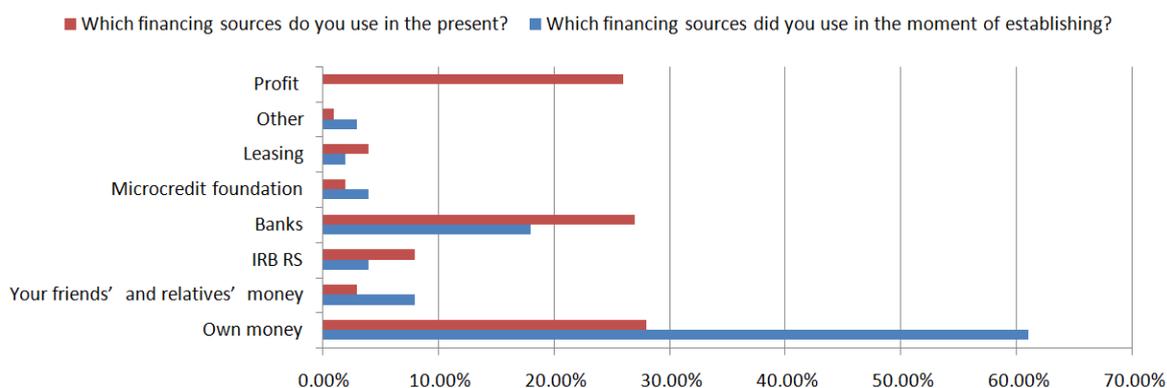
<sup>15</sup> It is not possible to calculate the mode of the number of employees in PLCs and enterprises with mixed ownership because the series of information does not contain the most frequent information (author's note).

of the enterprises that are PLCs and which have a mixed ownership belong to the group of medium enterprises, while IBEs are mostly representatives of micro enterprises.

### 4.3. Financial and Non-Financial Support to SME Sector

In the initial stages of their existence, small enterprises depend greatly on FaN support. We investigated which sources of finance the enterprises in the sample used when establishing the enterprise and which sources they use now.

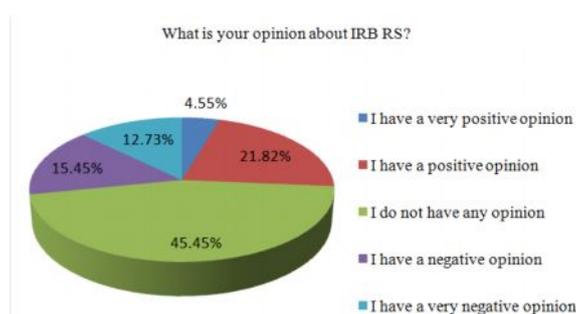
Fig 3: SMEs financing sources in the moment of establishing and today



Source: Author

In the past, people used their own money to establish an enterprise (61%) more than they do today (28%). Today, an enterprise profit is used to finance the enterprise (26%). Money from microcredit organizations was more often used for this purpose (4%) than today (2%) as they have more liberal conditions in terms of loans, but their interest rate is higher. Commercial banks are, for completely opposite reasons, a more significant source of finance today (27%) than they used to be in the past (18%). IRB RS is more present today (8%), but the bank was founded in 2006, which means that a large number of enterprises could not use it as a source of finance. The next question referred to respondents' views on IRB RS's work.

Fig 4: Respondents' views on IRB RS



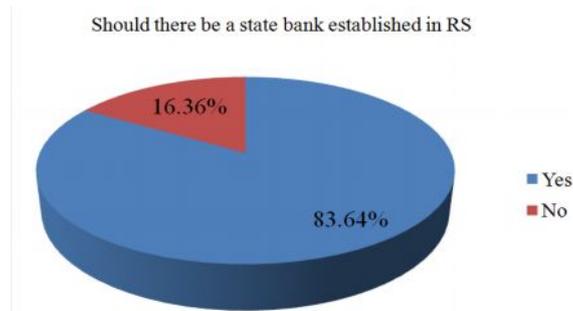
Source: Author

The fact that 45.45% of respondents have no clear opinion on IRB RS is to a certain degree unexpected. Only 26.37% of respondents are extremely pleased or pleased with IRB RS's work, even though their conditions regarding loans are no worse than in other banks.<sup>16</sup> There is a possibility that negative views of respondents toward IRB RS are caused by the insufficiently built image of IRB RS concerning placement of funds based on market principles. According to subjective views of some entrepreneurs from informal polls, the image of IRB RS is insufficiently built because there is a connection between the governing political structure and a great number of users of IRB RS's services.

<sup>16</sup> The interest rate is usually lower than in commercial banks (author's note).

Respondents were asked a leading question: “IRB RS’s interest rate consists of the output interest rate of IRB RS and the margin calculated by a business bank. Do you think that IRB RS should establish an independent sector of relations with their clients in order to lower the final (cumulative) interest rate, i.e. do you think that business banks should be excluded from the process of loan allocation financed by IRB RS?”. Four respondents (3.64%) did not answer this question, while 89 of them (90.91%) said yes. 17 respondents said no (15.45%). It is believed that those who said yes were persuaded by the possibility of lowering the interest rate, which is automatically acceptable.

Fig 5: Respondents’ views on whether it is necessary for a state bank to be established in RS

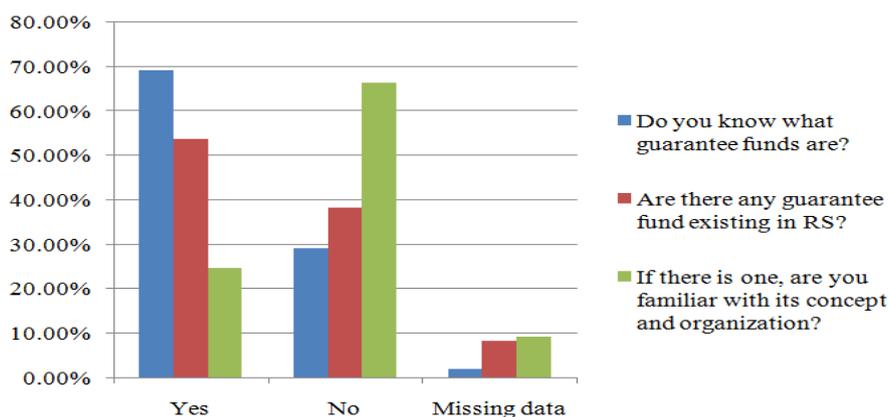


Source: Author

83.64% of respondents believe that there should be a state bank established in RS. Since July 9<sup>th</sup> 2013, there has been a state bank in RS called “Banka Srpske” and it was established in the process of recapitalization of “Balkan Investment Bank”. Here a few questions could be asked. Can a state bank contribute to improving banking services? Why do the majority of respondents support the establishment of a state bank? Can a state bank business be based on market principles or should it be oriented as a socially beneficial bank? Will a state bank field of operating overlap the IRB RS one? Should “Balkan Investment Bank” has been left to market mechanisms, which would have ruined the bank, and should the state have established a new, “healthy” bank if needed?

The several following graphs refer to respondents’ knowledge of entrepreneurial infrastructure.

Fig 6: Respondents' knowledge of guarantee funds concept and organization

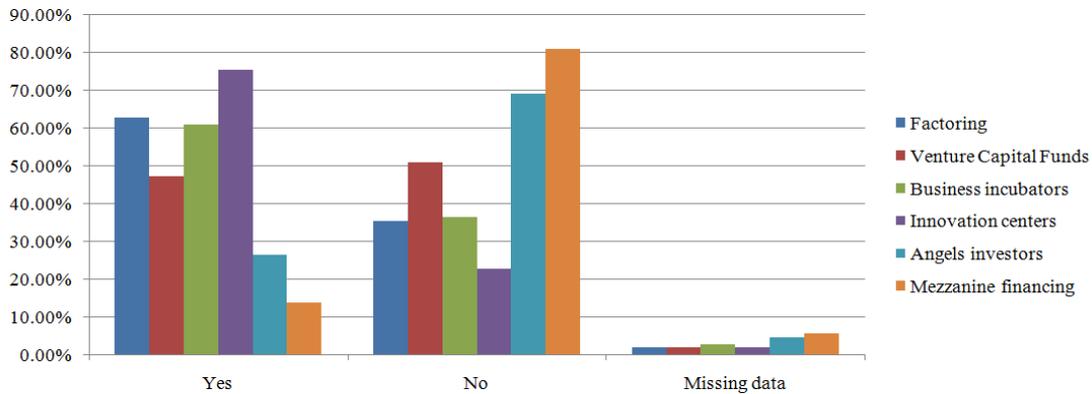


Source: Author

69.09% of respondents do know what guarantee funds are, while only 53.64% know that there is a guarantee fund in the Republic of Srpska. Only 24.55% of respondents are familiar with how guarantee funds function. Does the Guarantee Fund of the Republic of Srpska dedicate enough attention to building an image that potential users would recognize, or are users uninterested in the possibilities of the support offered on the market in the Republic of Srpska? A more detailed analysis would provide an answer to that question.

These are respondents' answers to the question whether they are familiar with specific forms of entrepreneurial infrastructure:

Fig 7. Respondents' knowledge about entrepreneurial infrastructure characteristics



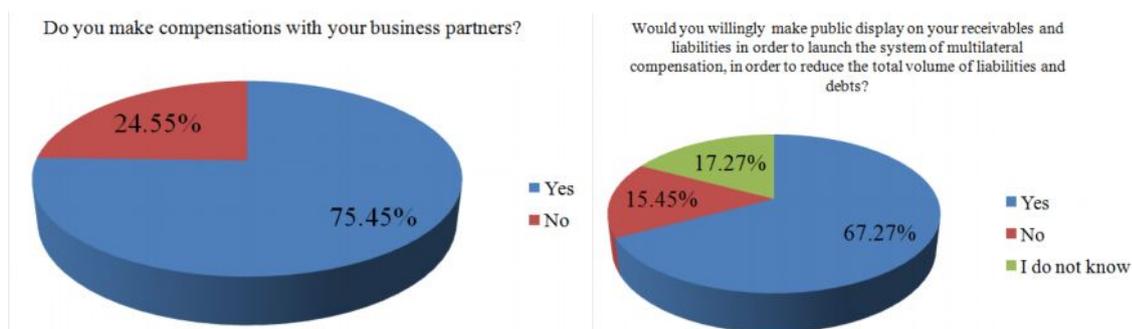
Source: Author

Innovation centers are the most “popular” among respondents (74.45%). Factoring (62.73%) and business incubators (60.91%) are also recognized by respondents as important elements of entrepreneurial infrastructure. It is a fact that the mentioned forms of entrepreneurial infrastructure do exist in the Republic of Srpska, with a tendency to increase. Having summed up respondents' views, there can be noticed that they are familiar with entrepreneurial infrastructures in the Republic of Srpska to the fullest extent.

Respondents were asked whether they would renounce their enterprise ownership in exchange for working capital, and if they would, what the percentage would be. Thirty-eight of them (34.55%) would renounce their ownership in exchange for working capital. Twenty-seven (79.41%) of those 38 would retain majority ownership, while 7 of them (20.59%) would renounce a part of the ownership larger than 50%. These facts show that in our entrepreneurial culture majority ownership represents more than a pure economic calculation, even though renouncing a part of the ownership could ensure an excellent perspective for an enterprise.

In the conditions of low liquidity of economy, enterprises often make compensations with their business partners. That is confirmed by the data from our research. Even 74.45% of respondents do it when possible. Respondents think that it is an acceptable business practice, which can be proved by the fact that 67.27% of respondents would willingly display their receivables and liabilities publically in order to launch a system of multilateral compensations. For that purpose, in February 2014 a Law on Single System for Multilateral Compensation and Cession was enacted (“Official Gazette of RS ” no. 20/14, 2014). This law still hasn't started being enforced.

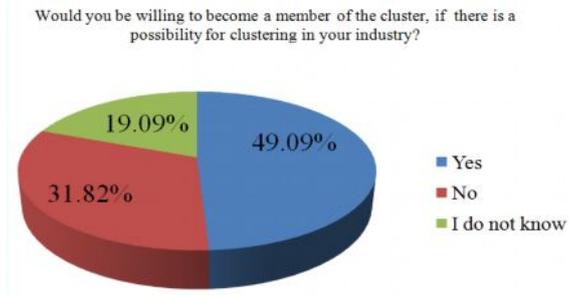
Fig 8: Respondents' opinion about compensations



Source: Author

Less than half of respondents are willing to become part of a cluster. Clusters make possible the fulfillment of some advantages on the market which manifest through the joint approach of several enterprises. The question arises why most of respondents (51%) do not want to cluster, or why they do not know whether they want it or not. Are respondents familiar with advantages that clustering brings?

Fig 9: The respondents' willingness to become members of a cluster



Source: Author

Even 21.82% of respondents do not know whether there is a local agency for the development of SMEs in their city/municipality, while 57.27% do. It shows that they are to a certain degree uninterested in the future of their enterprises but also that local development agencies are not very prominent.

#### 4.4. Testing the Hypothesis

By creating and mastering the models and instruments of FaN support to SME sector in the RS and providing the adequate business climate for their successful functioning, we will increase the availability of favourable financial means for SME, as well as the possibility of using the positive aspects of clusters, guarantee funds, factorings and other forms of entrepreneurship infrastructure” is the main hypothesis that is tested based on the results of the conducted research and certain other countries’ experiences presented in literature.

Instruments of FaN support to SME sector in RS are at a low level. Many developed instruments of FaN support to SME sector are not existent in RS at all (factoring, venture capital funds, angel investors, mezzanine financing). Entrepreneurs and managers in RS are not familiar with the existence of certain forms of entrepreneurship infrastructure. Even if they have some knowledge about their existence in other countries in the world, they are not familiar with how they function and how they influence SMEs. It is clear that entrepreneurs and managers of SMEs must invest in their education in order to become successful users of the SME sector supporting institutions. At the same time, it is necessary to provide a business climate that will stimulate, on a market basis, the development of models and instruments of entrepreneurial infrastructure, which will be useful for entrepreneurs and owners of SMEs.

Based on the responses, it is clear that there is a necessity for the existence of factoring organizations in the RS, as well as for the establishment of venture capital funds. The process of multilateral compensation was strongly supported by the respondents (67.27%), which requires the accelerated implementation of the Law on Single System for Multilateral Compensation and Cession. Mentioned before is in favor of confirming the basic hypothesis of this paper.

Certain SME support institutions in RS (IRB RS and the Guarantee Fund of RS) are still seen by the public as institutions closely connected to the authorities.<sup>17</sup> It is thought that their business is based on non-market principles, which to a certain degree diminishes the purpose of their existence. Respecting respondents’ opinion towards the exclusion of commercial banks from the process of IRB RS loans (80.91%), as well as fully affirming the positive role of the Guarantee Fund of RS would

<sup>17</sup> Still, a significant number of respondents support the existence of the state bank in the Republic of Srpska. That view arises from the belief that such a bank would provide better conditions for loans taking into consideration the general benefit of the society, while private banks interests are only of economic nature (author’s note).

increase the availability of credit funds for SMEs. The interest rates would decrease and Guarantee Fund would become a real guarantor for withdrawn loans to be returned.

When it comes to FaN support to SMEs in RS, it is interesting to mention Petkovic's research (2010, 291) in which the following assisting hypothesis is confirmed:

The creation of institutional and infrastructural assumptions of financing newly established and already existing SMEs in the form of initial and venture capital by financing from the debt and proprietary assets and transitional forms of finance will directly contribute to increasing the number of SMEs and economic restructuring in RS.

In the Republic of Croatia, according to CEPOR's data (2013, 37) which merged the results of numerous world researches in which Croatia is also included, the underdevelopment of informal forms of financing business venture launching is one of the most significant limitations of SME growth and development.

The research results mentioned previously show that there is a lot of room for developing forms of financial and non-financial support to SME sector in RS, as well as changing entrepreneur's views on the role and importance of certain support instruments. Therefore, we consider the main hypothesis to be confirmed.

## 5. CONCLUSION

If we wanted to determine what the majority of the world developed economies have in common, we would come to the conclusion that it is developed SMEs. In order to generate long-term development, it is necessary to continue to develop instruments of financial and non-financial support to SME sector.

Analyzing the results obtained by the empirical research conducted on the sample of 110 respondents in five cities and 14 municipalities in RS, we have come to some very important conclusions. Only 26.37% of respondents are very pleased or pleased with IRB RS's work, even though conditions regarding loans are not worse than they are in other banks (the interest rate is mostly lower). There is a possibility that the negative view they have on IRB is caused by the insufficiently built image of IRB concerning the placement of funds based on principles of the market. Eighty-nine respondents (80.91%) think that it is necessary to exclude commercial banks from the process of IRB RS loan allocation and therefore lower the total output interest rate. As much as 83.64% of respondents think that the existence of a state bank is necessary in RS.

The percentage of 69.09% of respondents are familiar with the notion of guarantee funds, while only 53.64% are familiar with the fact that there is a guarantee fund in RS and 24.55% are familiar with how the fund works.

When it comes to entrepreneurial infrastructure, innovation centers are the most popular among respondents (74.45%). Factoring (62.73%) and business incubators (60.91%) are also recognized by respondents as important elements of entrepreneurial structure. It is a fact that the mentioned forms of entrepreneurial infrastructure do exist in RS with a tendency of increasing. Having summed up respondents' views, we notice that they are to the fullest extent familiar with the forms of entrepreneurial infrastructure in RS. Thirty-eight (34.55%) respondents would renounce their ownership in exchange for working capital. Twenty-seven (79.41%) of those 38 would retain majority ownership, while seven of them (20.59%) would renounce a part of the ownership larger than 50%.

Even 74.45% of respondents make compensations when possible. Respondents think that it is an acceptable business practice, which can be proven by the fact that 67.27% of respondents would willingly display their receivables and liabilities publically in order to launch a system of multilateral compensations. Less than a half of respondents are willing to become part of a cluster. Clusters make possible the fulfillment of some advantages on the market which manifest through the joint approach of several enterprises. The percentage of 21.82% of respondents in the sample do not know whether there is a local agency for SME development in their city/municipality.

Certain development in the field of enhancing instruments and models of financial and non-financial support to SME sector in RS can be achieved by consistently enforcing the Law on Single System for Multilateral Compensation and Cession ("Official Gazette of RS" no. 20/14, 2014) as soon as possible and motivating enterprises to cluster. According to the data from the Central Bank of Bosnia and Herzegovina ([www.cbbh.ba](http://www.cbbh.ba)) only two companies in Bosnia and Herzegovina at the

moment offer factoring services and both of them are located in the Federation of Bosnia and Herzegovina. That means that there are no factoring companies in the Republic of Srpska. Institutions of the system should create an environment that would motivate the establishment of factoring companies by foreign and local investors.

In order to lower the total output interest rates in IRB RS, we think that it is necessary to exclude commercial banks from the process of loan allocation. IRB RS could establish a sector of its own which would work with final beneficiaries, therefore substituting the role of commercial banks in the process of loan allocation. The new role of IRB RS would probably motivate commercial banks to lower their interest rates and simplify the procedure of loan allocation for SMEs and entrepreneurs.

The analysis of our research results and the comparison with empirical results of other researches enabled achieving scientific and social goals of this paper. Based on the review of literature and the analysis of the empirical research results, we think that we succeeded in proving the set hypothesis and the conclusion is that by creating and mastering the models and instruments of FaN support to SME sector in the RS and providing the adequate business climate for their successful functioning, we will increase the availability of favourable financial means for SME, as well as the possibility of using the positive aspects of clusters, guarantee funds, factorings and other forms of entrepreneurship infrastructure.

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