

## **The impact of SMEs in the economic development of Kosovo**

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### **Abstract**

The vast majority of enterprises around 98% operating in Kosovo are micro-, small- and medium enterprises. In 2012, SMEs provide 80% of jobs from all companies.

Therefore, SMEs are the biggest contributor to economic growth and employment and generate the bulk of the state budget. Therefore, development of SMEs is one of the most important aspects for economic growth and competitiveness. Legal and institutional reforms have led to a system that enables the rapid and free development of SMEs in the market, and tax policy and tax rates are among the lowest in the region. Medium-term strategy for development of SMEs defines different priorities and policy measures for the development and growth of SMEs.

**Keywords:** Management, SME, development, strategy, economics.

### **Introduction**

The impact of SMEs in Kosovo's economic development has to do with the very important field of accelerating economic growth in Kosovo. Kosovo has gone through very difficult periods and has experienced significant material damage, destroyed enterprises during the war. SMEs are the basis of economic development and growth and need great support by the government of Kosovo. This paper will explore the positive and negative aspects of the development of SMEs.. Kosovo needs the experience of EU countries and other developed countries and well educated experts to be integrated into the business, in order to create a successful business. SMEs are carriers of economic development and job openings, which also reduce unemployment, which is one of the biggest problems in Kosovo.

### **The importance of SME development for the economy of Kosovo**

Kosovo SMEs faces numerous challenges. Currently the sector is weak and not competitive. More than half of SMEs are involved in retail and 10% in manufacturing, while products are not competitive in the markets of the region and the EU. This situation is a factor for reducing the economic growth, after considering the number of new job seekers entering the labor market every year, it is estimated that economic

growth would need at least 7%.

The lack of functional bankruptcy system negatively affects the reliability and economic governance, resulting in attracting FDI, also directly affects and damages fair competition and presents obstacles to combating the informal economy.

Lack of policies for the development of industry sectors, access to finance, inadequate physical infrastructure and public still hinders the development and growth of SMEs, taking into account the need to increase local production in the future.

By 2020, Kosovo will develop and implement policies on sustainable development of industry and SMEs. We will also establish a fully functioning system of bankruptcy. This will be complemented with the implementation and enforcement of secondary legislation and legal and operational mechanisms including mechanisms for alternative dispute resolution, such as arbitration that are able to ensure the effective implementation of business contracts.

Horizontal active industry policy will contribute to increasing the competitive capacities without creating distortions in the market.<sup>1</sup>

### **Importance of Small and Medium Enterprises in the market economy**

SMEs have very long history, and their development is marked by expansion and their occasional stagnation. SMEs demonstrate a high degree of innovation, flexibility and adaptation to changes that occur in the environment. SMEs are market-oriented local economies. In economic literature developed countries singled out four factors contributing to the SME market economy:

1. Contribution to the processes of technological change;
2. Contribution to the behavior of healthy competition;
3. Creation of new jobs;
4. Offer rich products in the local market.

SME development also contributes to the transition countries in the wake of entrepreneurial initiative to change the economic structure and harmonious functioning of the economy in general. Great importance is paid to employment of workers in which SMEs occupy a very important place in the economy of the country. Based on the above findings for small and medium enterprises in some countries it can be concluded that:

- SMEs gain great importance in the market economy countries;
- The importance of SMEs lies in the job openings;
- SMEs have an important role in the field of innovation, improvement of structures, and improved offers in the development of entrepreneurship;
- SMEs contribute to economic efficiency of national economies and international exchanges of products and services.

The contribution of SMEs to the national economy associated with positive impact on employment creation through forms dealing with self-employment. Around 60-70% of new jobs in the OECD countries (most developed countries of the world) are based on SMEs. The impact on the growing importance of SMEs come mainly from

<sup>1</sup> The national strategy for European integration “ Kosova 2020 “ p. 45-46.

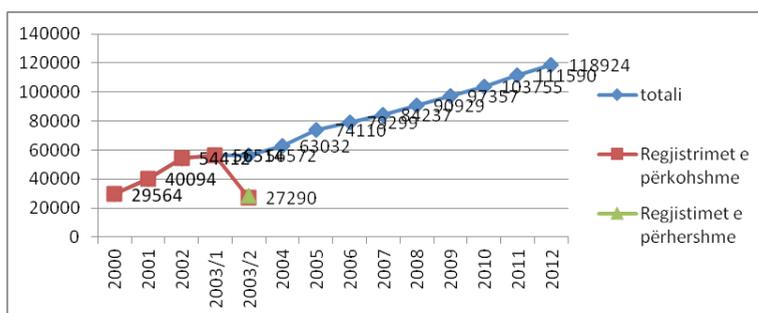
the increased share of services sector, construction and information technology, which require great flexibility to market demands which are much more prepared to offer SMEs (Mustafa, Kutllovci, 2006, 25).

By 2020, Kosovo will have a competitive market economy. So for this purpose sources of financing should be more accessible and more favorable and provide local market competition, improve research and development and develop a productive social dialogue.<sup>2</sup>

### Review of the current situation of SMEs and obstacles to their development

Today the private sector in many developed countries and those in transition is the source of generation of new jobs and income growth. Therefore, SMEs are the motor force of economic growth and development around free market economies including almost all countries in the region. Kosovo is going through a period of transition, where the development of the private sector is playing and will play a crucial role in the recovery and development of the local economy. Most private initiatives and family businesses, experienced a fast expansion in these transition years, especially in the trade sector. The development of SMEs in the field of trade and services and less on the productive sector and exporter is due to unfavorable macro-economic policies (taxes, credit market and public services) which have not been favorable for new industries and SMEs. Unprofessional management of SMEs and irresponsibility in managing social enterprises in the postwar period in Kosovo resulted in a bad efficiency of the enterprise. Private enterprises in Kosovo are not able to cross the boundaries of micro or small enterprises, most of the programs of these enterprises are not oriented towards concept complementary sectors of sustainable economic development in Kosovo such as energy, mining, minerals, post-telecom etc, and this orientation can not be considered an alternative. In the below table, is presented the trend of businesses in Kosovo.

Trend of business registration in Kosovo during the period 2000-2012



Source: Agency for Registration of Businesses in Kosovo

<sup>2</sup> The national strategy for European integration " Kosova 2020 " p. 42.

## Current situation of SMEs in Kosovo

SME development in Kosovo is considered satisfactory, because they constitute about 98% of the total number of enterprises, and privatization is still unsatisfactory and has poor economic effects. SMEs are oriented towards domestic competition and not towards the EU. And as such, they are not export-oriented, which hinders their contribution to GDP, creation of new jobs and economic development. About 50% of all SMEs in Kosovo operate in the trade sector, which is characterized by small investments. Less than 10% of Kosovo SMEs operate in the manufacturing sector.<sup>3</sup> The Government of Kosovo in cooperation with other local and international institutions has prepared a package of laws, some of which were approved, some of them are still in the parliamentary procedure of adoption. The lack of proper legal reforms and the establishment and operation of SMEs in Kosovo, the lack of macro-economic policies that support private sector development and especially SMEs, is hindering the smooth functioning and development of SME. Informality is another negative aspect in Kosovo. It prevents genuine competition, and weakens worker protection by reducing trust between SMEs and financial institutions, discourage foreign investment, etc. The main barriers addressed by the private sector are the lack of proper financial institutions-banks, lack of control system, the collapse of the former large SMEs, the extension of the privatization process and operational questionable policies. SMEs also face other problems such as lack of electricity, unfair competition, problems with transport and telecommunications, education and management skills etc.

Kosovo has signed agreements in the area of trade liberalization with countries in the region, such as Albania, Macedonia, Croatia and Bosnia and Herzegovina. Kosovo lacks practice and application of different mechanisms and financial instruments. The only mechanisms to give SMEs access to finance in addition to informal sources are micro-finance institutions and commercial banks credit lines which are still expensive and often too bureaucratic. Meeting the requirements of the SME sector for loans by commercial banks is improving although it is still low in comparison with other countries.

## The role of SMEs in the economic development of Kosovo

Since 1999, the domestic economy has been largely driven by international aid and remittances (World Bank, 2010). The role of the private sector, particularly SMEs has been relatively weak. However, Kosovo is traveling towards a modern economy with free trade, economic growth and development. Currently, there are unfavorable business environment, and in the absence of creative and entrepreneurial culture. The economy is constantly changing, providing opportunities for new businesses. Demand for services is 'booming' and is growing, and approximately 97% of services firms are small with fewer than 100 employees.

Entrepreneurship is a dynamic process of creating a rich growth is the process of

<sup>3</sup> Based assessment of the economic region sud 2014 faqe 11

initiating a business venture by organizing the necessary resources assuming the risk and rewards associated with. SMEs have a direct impact on changes in technology, and bring healthy competition, opening new jobs and rich product offering in local markets. SMEs are characterized as flexible, with a direct relationship to work, employment opportunities are managed by one person, limited capital, innovations etc. Economic growth is linked to the growth of SMEs which stimulate competition, providing new products and services and other advanced services to survive market only (Action Plan of the European Partnership, 2013). SME development offers many job opportunities which can help reduce unemployment and demographic challenges facing these populations, which are growing rapidly. In addition, the development of the SME sector can contribute to strengthening competitiveness and productivity, promoting revenue growth both global and per capita income.

This development promotes the transformation of the SME sector, due to its link with innovations and technological development. On the other hand, this process contributes to regional and local development, as well as social cohesion, enabling the reduction of inequalities, because income growth of a wide segment of the population will reinforce demands for better governance.<sup>4</sup>

### **Strategy for private sector development in Kosovo 2013-2017**

Strategy of Development of Private Sector in Kosovo 2013-2017 addresses issues such as:

- Development of Small and Medium Enterprises;
- Promotion of investment;
- Internal Market;
- Free Movement of Goods;
- Foreign trade policies.

The aim of the strategy is to address the challenges and adopt changes dealing with the development of industry and private sector, which are changes in the legal framework, institutional and policy. Changes foreseen in the Strategy for the Development of the Private Sector 2013 - 2017 are important, because they are dealing with the commitment of the Ministry and relevant institutions to implement more stringent policies on capacity building for improving the environment, that would make Kosovo competitive with regional countries

In line with the goals of MTI for the respective period, the strategy focuses on the adoption and implementation of policies that would contribute to the improvement of domestic production and competitiveness of Kosovo in the European market. Ministry of Trade and Industry will continue its work based on guidelines stemming from this important strategic document, always remained committed to the overall goal of sustainable economic development of the Republic of Kosovo. The strategy of the Ministry of Trade and Industry for the Development of the Private Sector in an effort to boost employment and reduce poverty, that aims to create a globally

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<sup>4</sup> Report on the role of small and medium enterprises in the Mediterranean (2012) 3.

competitive private sector. The strategy provides a framework for possible intervention by the central and local government, private sector and non-governmental. These interventions inspire changes necessary for achieving social welfare, modern infrastructure, a sustainable economic development, and provision of effective public services.

This strategy is organized into three pillars:

- The development, support and promotion of investments and businesses;
- Improving the free movement of goods or regulation of the Internal Market;
- Advancement of Trade Policy.

This strategy is based on the pillar of sustainable economic development program of the Government of the Republic of Kosovo (2011- 2014).

### Conclusions and Recommendations

Based on a research conducted by ABR, ATK, associations and other institutions indicate that over 98% of enterprises in Kosovo are SMEs which contribute strongly to the economic development of Kosovo; More than half of SMEs are involved in commercial activities, while 10% of them already are part of production activities. There are large differences in terms of business ownership by gender. Research shows that only 6% of businesses are owned by women that shows the low level of female entrepreneurial activity. According to research in years 2010-2011 appears that SMEs contribute 75.97% to the creation of jobs and 43.3% of GDP. It is recommended also a higher integration of women in the management of SMEs, business facilitation of approaches by removing excess load laws and regulations, close cooperation between the Government of the Republic of Kosovo, Ministry of Trade and Industry and Business Support Agency with entrepreneurs.

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