

The business environment in the transition region

Governments across the transition region are continuing to improve the local business environment in an attempt to unleash the full productive capacity of the private sector. This report summarises feedback from the managers of firms in 29 transition countries about what they regard as the main improvements – and the remaining challenges – in the business environment that they experience on a daily basis. Across the board, managers reported that they were most constrained by (i) unfair competition from the informal sector, (ii) limited access to credit and (iii) expensive or unreliable electricity supply.

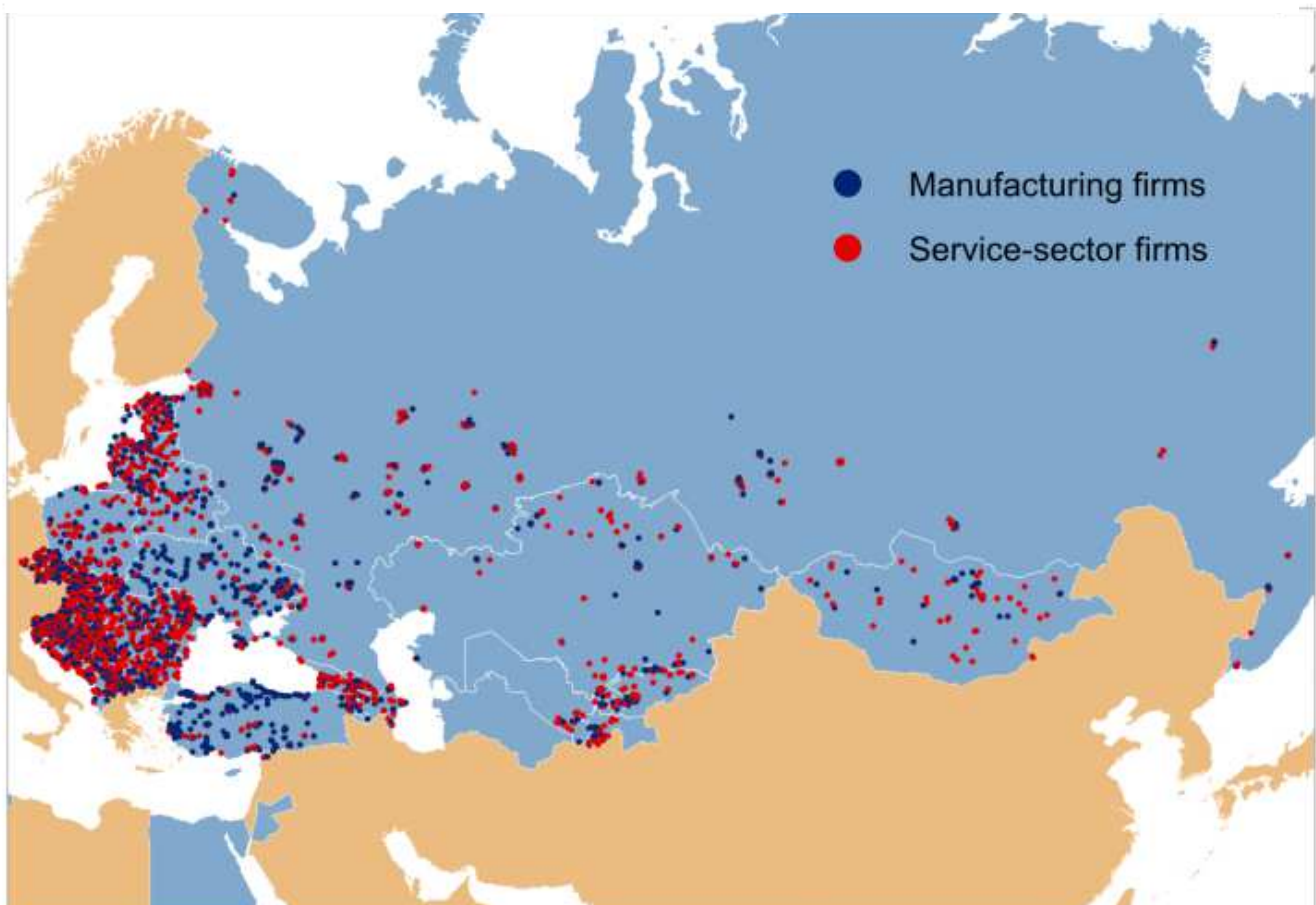
Introduction

In the wake of the global financial crisis, governments in the transition region are continuing to search for ways to resuscitate economic growth. One course of action is to create a more conducive business environment, which can boost growth by establishing competitive and fair conditions for all businesses.

This report summarises the key results of the fifth round of the Business Environment and Enterprise Performance Survey (BEEPS V), which was conducted by the European Bank for Reconstruction and Development (EBRD) and the World Bank Group in 29 countries. The survey was conducted in Russia in 2011-12 and in 2013-14 in all other countries. Senior managers were interviewed at more than 15,500 randomly selected firms. Those firms – all of which had at least five employees – spanned 29 of the EBRD's countries of operations. Chart 1 shows the geographical coverage of the BEEPS V survey.

Managers were asked for their views on topics such as infrastructure, competition, sales and supplies, labour, innovation, land and permits, crime, finance, and relations between business and government. They were also asked about the management practices in their firms.

Chart 1. Location of firms surveyed for BEEPS V



Source: BEEPS V.

Note: BEEPS V was conducted in 2013-14 (2011-12 in Russia)

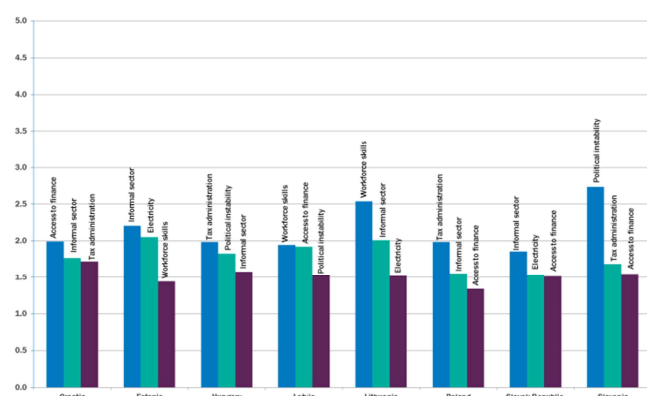
Main trends

In BEEPS V, the top three obstacles identified by firms in the transition region were (i) competitors' practices in the informal sector, (ii) access to finance and (iii) electricity. In BEEPS IV, which was conducted in 2008-09, the same three obstacles made up the top three, with access to finance and competitors' practices in the informal sector switching places. Chart 2 shows the top three obstacles in each country according to BEEPS V.

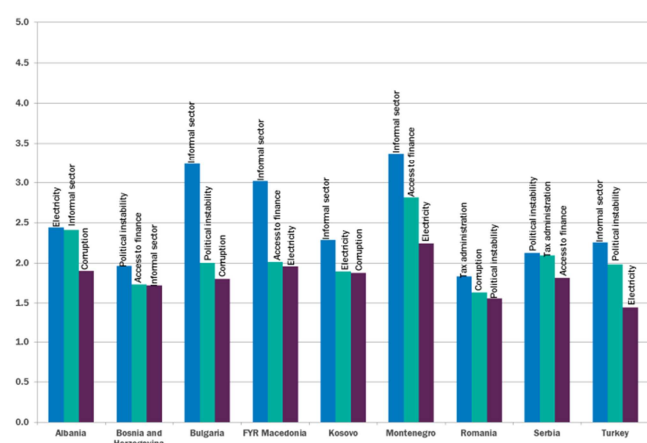
It is important to note that the analysis is based on constraints as perceived by each firm. As such, it can only indicate policy priorities and cannot be used to rank countries by the quality of their business environments.ⁱ

Chart 2. Top three obstacles in each country

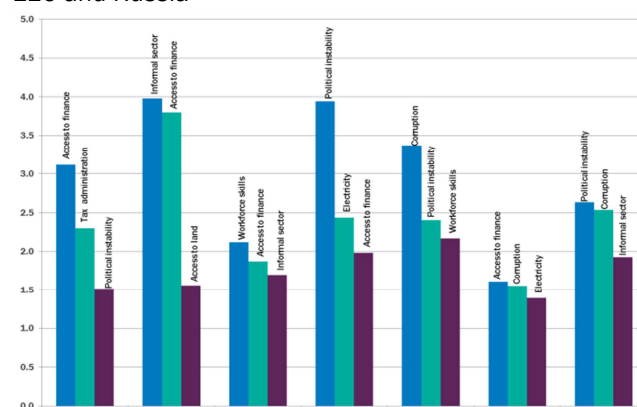
CEB countries



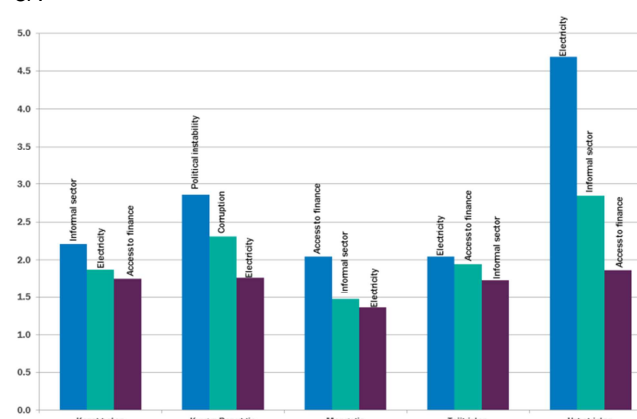
SEE countries and Turkey



EEC and Russia



CA



Source: BEEPS V and author's calculations.

Note: BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Informal sector

Firms in almost a third of all countries considered competitors' practices in the informal sector to be the biggest obstacle. There were just nine countries where the informal sector was not one of the top three concerns, and it was in the top eight in all countries. This issue transcends regional boundaries, being the main constraint from Azerbaijan to the Slovak Republic. The shadow economy is more than just unregistered firms. Registered firms often under-report their income, hide employees or fail to declare wages (termed "envelope wages") to avoid taxes or the need for documentation. Such activities are widespread in businesses that deal largely in cash, such as small shops, bars and taxi companies, as well as firms in the construction, agriculture and household services sectors.

Access to finance

Access to finance was also regarded as a major constraint. It was the top constraint in Armenia, Croatia, Russia and Mongolia, and it was among the top three in another 14 transition countries. Given that BEEPS V was conducted at a time when many banking sectors were still recovering from the severe effects of the global

financial crisis, this is hardly surprising. In virtually all countries, the percentage of firms with a loan or a line of credit fell by comparison with BEEPS IV. Limited access to finance is a particularly acute problem for firms younger than five years. This was driven by a substantial decline in demand for credit, with only a small reduction being seen in the supply of credit.

Electricity

Electricity issues were the main obstacle in Albania, Tajikistan and Uzbekistan, and they were among the top three in a further 12 transition countries. The underlying reasons differed across countries. In Central Asia, it was mostly to do with unreliable electricity supply, which was characterised by frequent and costly power outages. In central Europe and the Baltic states (CEB), on the other hand, it stemmed from high electricity prices.

Different firms, different complaints

Not all types of firm complain about the same aspects of the business environment. The retail sector, for instance, is typically more exposed to the shadow economy than the manufacturing sector, especially when it comes to smaller firms. Moreover, young firms play a particularly important role in creating jobs, so it is important to understand which types of obstacle they consider to be the most problematic.

In BEEPS V, young firms were most constrained by limited access to finance, rather than competitors' practices in the informal sector. This was the case in all regions, with the exception of south-eastern Europe (SEE) and Turkey. In the presence of relatively strict collateral requirements, and stringent lending procedures more generally, young firms with a limited track record find it particularly difficult to demonstrate their creditworthiness and obtain loans in order to continue growing. While policy-makers have implemented many programmes focusing on SMEs' access to finance, hardly any of those programmes specifically support young firms.

In the CEB region, where corruption tends to be less prevalent, onerous tax systems were a major obstacle for young firms. This often related to the time that it took to fulfil tax obligations.

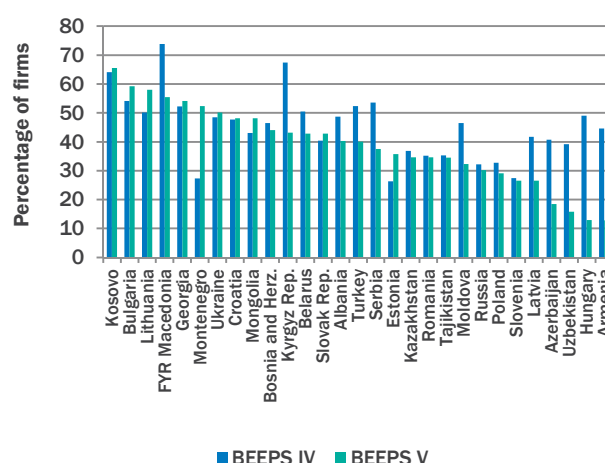
Large firms, on the other hand, complained most about electricity – particularly firms in Central Asia and Russia. In CEB countries, which have fairly strict labour regulations (particularly for permanent employees), those regulations were the second biggest obstacle. Many of these countries were hit hard by the global financial crisis, and the fact that those strict laws prevented firms from adjusting the number of workers in line with shrinking demand may explain this result.

Competitors' practices in the informal sector were the top constraint for retail-sector firms in transition countries, while manufacturing firms complained most about limited access to finance.

Informal sector

Competitors' practices in the informal sector were the main obstacle reported by firms in BEEPS V. Almost 40 per cent of all firms mentioned that they faced competition from unregistered firms or other informal-sector activities, with that percentage ranging from 12.8 per cent in Armenia to almost two-thirds in Kosovo (see Chart 3). In several countries, mostly in Central Asia, that percentage declined substantially relative to BEEPS IV. In the SEE region, it fell from almost three-quarters to 55 per cent in FYR Macedonia, but it almost doubled in Montenegro, where it stood at 52.4 per cent.

Chart 3. Competition from the informal sector



Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Although unregistered firms can still be found in transition countries, these days the motivation for engaging in informal-sector activities stems mainly from *registered* firms' desire to evade tax by under-reporting income or not fully declaring employee numbers or wages. In the last few years, several transition countries have made it much easier to officially establish a business by setting up one-stop shops and reducing registration costs. However, it may take a while to convince unregistered firms to register and reduce the informal-sector practices used by registered firms.

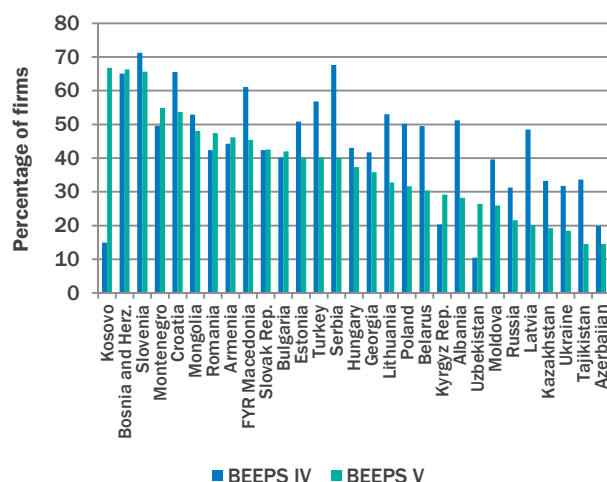
The shadow economy can make entrepreneurship less profitable, hamper investment (by restricting access to credit), undermine broader private-sector development and reduce social protection, thereby stifling economic growth and prosperity. On the other hand, the shadow economy can also provide an outlet for economic activity (mainly in the form of small and medium-sized firms) that is unable to flourish in the face of excessive barriers to enterprise in the formal sector.

Access to finance

Use of bank credit

Chart 4 shows the percentage of firms that reported having a loan or a line of credit in BEEPS V, comparing those figures with the data for BEEPS IV. That percentage fell in most transition countries. In Albania, Latvia, Lithuania and Serbia, it declined by more than 20 percentage points. The largest average declines were recorded in the CEB region and Turkey – the transition countries that have the strongest ties to the global economy. Consequently, they were also the most strongly affected by the global economic crisis.

Chart 4. Firms with a loan or a line of credit



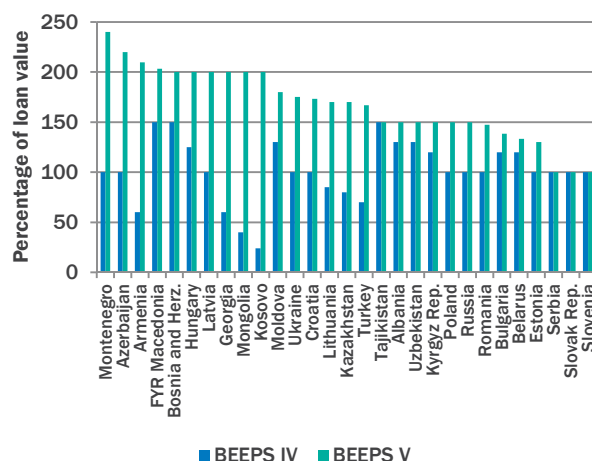
Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

The SEE region includes both countries that saw large increases in the percentage of firms with a loan (such as Kosovo and Montenegro) and countries with large declines (such as Albania and Serbia). There are several reasons for these differences. Firms in Kosovo used to rely more on friends and family for funds, being supported by significant inflows of remittances. However, when the global financial crisis struck and remittances declined, they turned more towards banks. Moreover, Kosovo declared its independence from Serbia in February 2008 and several banks have entered the market since then, competing for market share and improving the availability of credit in the process. Albania, FYR Macedonia and Serbia, on the other hand, have had high levels of non-performing loans for a long time, and lending activity has declined owing to deleveraging by Western (particularly Italian and Slovenian) banks. It has also been affected by the problems of Greek banks, which have a significant presence in all of those countries.

Increase in required collateral

Chart 5 shows that the median collateral required for financing has increased in virtually all countries as a percentage of loan value. This has made it more difficult for firms, in particular the younger ones, to access bank credit.

Chart 5. Borrowing firms: median collateral required



Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Lower demand for credit or less supply?

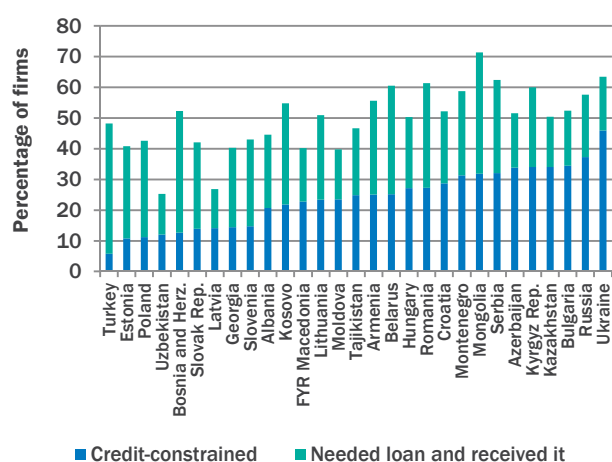
The percentage of firms that had applied for a loan also decreased substantially, declining by almost a third compared with BEEPS IV (falling from 38.1 per cent to 24.7 per cent). This suggests that part of the deleveraging process across the transition region is demand-driven. In the aftermath of the crisis, many firms have revised their investment plans downwards or abandoned them altogether, so they no longer have any need for a bank loan. A clear and unambiguous measure of whether firms are credit-constrained can be created by combining firms' answers to various BEEPS questions. Credit-constrained firms are defined here as those that need credit but have either decided not to apply for a loan or were rejected when they applied.

Almost half of all firms surveyed in BEEPS V reported needing a bank loan. A total of 47.5 per cent of them turned out to be credit-constrained. In BEEPS IV, 60.3 per cent of surveyed firms needed a bank loan, with 45.7 per cent of them being credit-constrained. Taken together, this indicates that there was a fairly substantial decline in demand for credit and only a small reduction in supply.

There was, however, substantial variation across countries (see Chart 6). Demand for credit decreased everywhere, except Hungary, Kosovo and Romania. In contrast, the percentage of credit-constrained firms increased in almost two-thirds of countries relative to

BEEPS IV. Particularly strong declines in access to credit were observed in Ukraine and Russia (both of which saw increases of more than 20 percentage points in the percentage of credit-constrained firms), followed by Slovenia, Croatia and Lithuania. At the other end of the spectrum were countries where the percentage of credit-constrained firms decreased relative to BEEPS IV. The largest decline was seen in Kosovo, where that percentage fell from 72.2 per cent to 39.8 per cent owing to the entry of new banks following the declaration of independence from Serbia in February 2008.

Chart 6. Credit-constrained firms



Source: BEEPS V and author's calculations
 Note: BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Limited access to credit may not only constrain firm growth in the short term, but may also have longer-term negative effects. BEEPS results show that where banks ease credit constraints, firms tend to innovate more by introducing products and processes that are new to their local and national markets.

Electricity

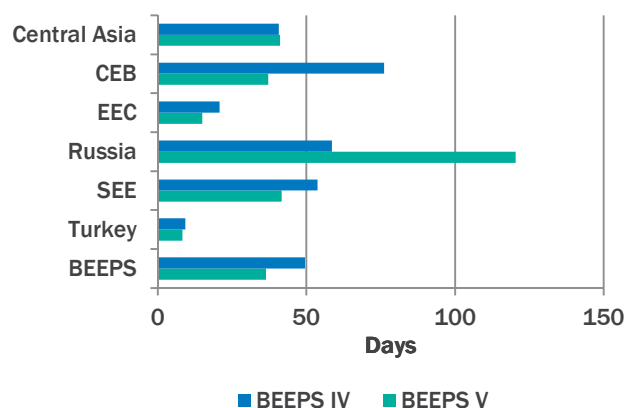
Issues related to electricity remained the third largest obstacle to firms in BEEPS V. However, looking at the transition region as a whole, some improvements have been made since BEEPS IV. The average time that it takes to be connected to electricity fell from 49.5 days in BEEPS IV to 36.3 days in BEEPS V, while 38.4 per cent of firms reported experiencing power outages in BEEPS V, compared with 43.7 per cent in BEEPS IV. In addition, the average number of power outages decreased from 6.4 to 5.2 per month, and they lasted almost an hour less on average (3.7 hours, compared with 4.6 hours in the previous round). That being said, the percentage of firms reporting that informal gifts and payments had been expected or requested in return for being connected increased from 10.7 per cent in BEEPS IV to 12.1 per cent in BEEPS V.

There remain, of course, significant differences across countries and regions. In Turkey and several CEB countries, industrial electricity prices increased before and/or during the period of the survey, leading companies to complain about electricity issues, even though the time it took to be connected was relatively short, the percentage of firms reporting power outages was low and the percentage of annual revenue that was lost owing to power outages was lower than in some other regions. In Central Asia, on the other hand, firms still have to deal with an unreliable electricity supply, frequent power outages and corruption when it comes to being connected.

Being connected to the grid

Firms in Turkey had to wait an average of just eight days or so to be connected to electricity. Meanwhile, firms in the CEB region saw average waiting times decline the most (from 76 to 37 days) between the two BEEPS rounds (see Chart 7). There are several explanations for this. First, these countries joined the EU in May 2004, adopting the first and second EU electricity liberalisation directives. They were therefore required to take a minimum number of steps towards the liberalisation of their national markets by certain key dates. Second, around 2007 EU member states began to exchange best practices in terms of the procedures required to get connected to electricity, and progress was made following the establishment of the Agency for the Cooperation of Energy Regulators in 2010. Third, there were improvements in the resources and abilities of most national energy regulators during this period. Estonian firms, in particular, saw a vast improvement in the time taken to get connected – from over 200 days in BEEPS IV to just 15 days in BEEPS V. This reflects that 35 per cent of the electricity market was liberalised in 2009 (at which point customers using at least 2GWh/year could choose their electricity supplier) with full liberalisation following in 2013.

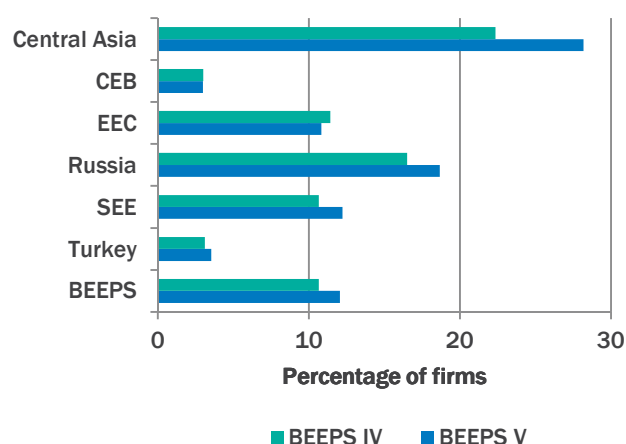
Chart 7. Waiting time to be connected to electricity



Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

In Russia, however, the average waiting time doubled, from 58.6 days to over 120 days, giving officials ample opportunity to seek informal payments. Indeed, 11.4 per cent of Russian firms reported that an informal payment was expected or requested when they applied to be connected – second only to Central Asia (see Chart 8). According to the World Bank's *Doing Business* report for 2014, Russia has since made it easier to get connected, setting standard connection tariffs and eliminating many of the procedures that were previously required, so an improvement can be expected in the next BEEPS survey.

Chart 8. Informal payments to be connected to electricity



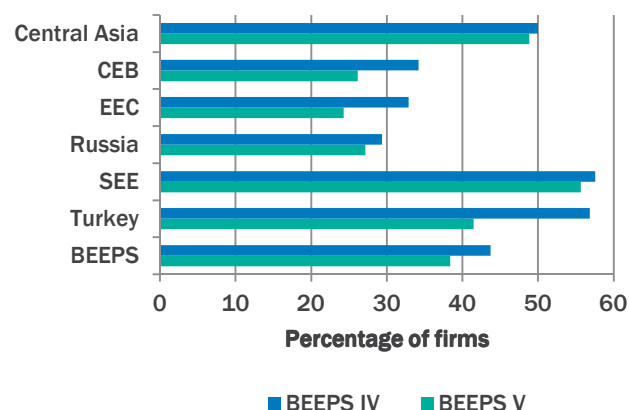
Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Compared with BEEPS IV, the percentage of firms reporting informal payments were expected or requested increased most strongly in Central Asia – particularly in Mongolia, the Kyrgyz Republic and Kazakhstan.

Reliability of electricity supply

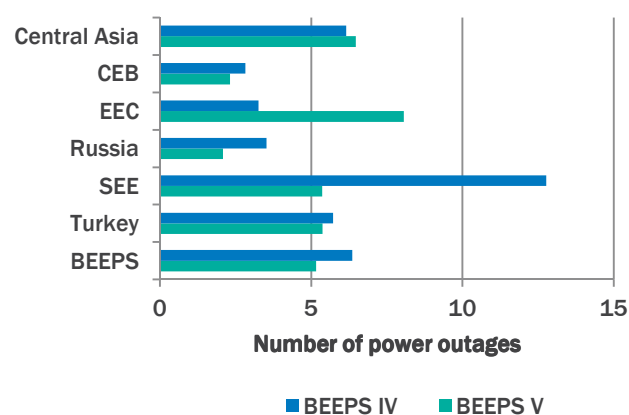
Firms in Central Asia also had to deal with more than their fair share of power outages, with almost half of them experiencing outages. While power outages were, on average, experienced by a larger percentage of firms in the SEE region (see Chart 9), Central Asia came out on top – followed by Turkey and the SEE region – in terms of the number of power outages in a typical month, their duration and the losses resulting from them (see Charts 10 to 12).

Chart 9. Firms that have experienced power outages



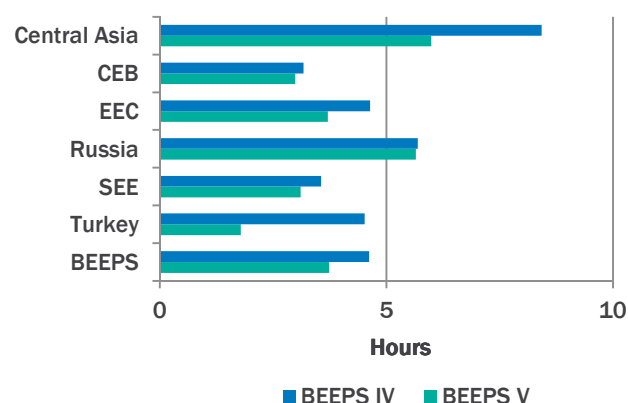
Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Chart 10. Number of power outages in a typical month



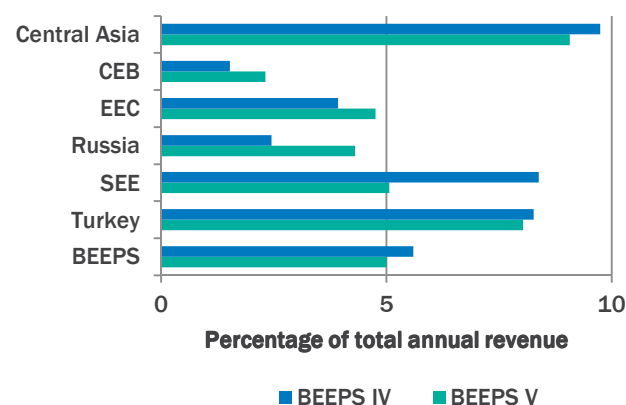
Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Chart 11. Duration of power outages



Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

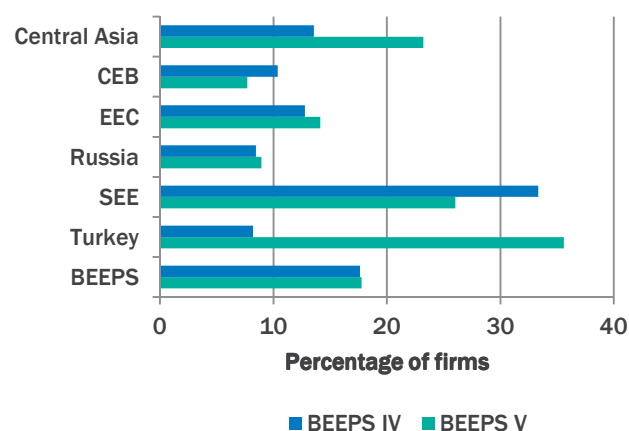
Chart 12. Losses due to power outages



Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Nevertheless, several SEE countries (such as Albania) have seen improvements in the reliability of their electricity supply, partly owing to increased precipitation. Most Central Asian countries have to deal with transmission bottlenecks, as well as ageing power plants. While they are addressing those problems to the best of their abilities, at least some of the improvements seen since the last BEEPS survey can be attributed to a higher percentage of firms (23.2 per cent, up from 13.6 per cent) taking matters into their own hands by owning or sharing an electricity generator (see Chart 13). In Turkey, the substantial increase in the percentage of firms that own or share a generator can partly be explained by the fact that they are able to sell surplus electricity from renewable generators to power distribution companies since December 2010.

Chart 13. Firms that own or share an electricity generator



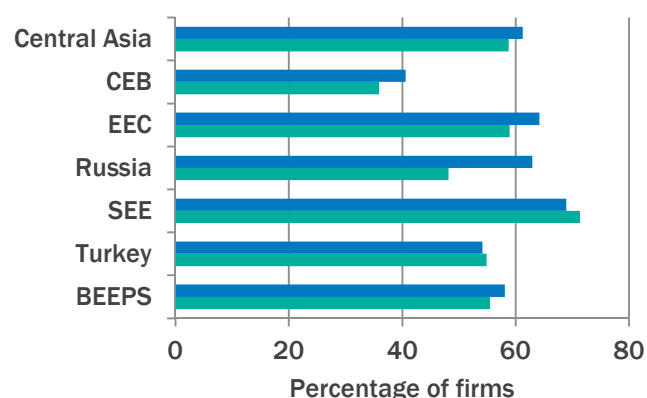
Source: BEEPS IV and V and author's calculations
 Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Tax administration

Tax administration was among the top three obstacles in 7 of the 29 countries in BEEPS V, as it had been in BEEPS IV. It remained the top obstacle in Romania, it became the main constraint in Hungary and Poland, and it was considered to be the third largest obstacle overall by firms in the CEB region.

This does not appear to be caused by the carrying out or frequency of tax inspections, or the fact that informal payments were expected or requested during inspections or meetings with tax officials – although increases have been observed for some of these things in certain countries. The percentage of firms that had been visited or inspected by tax officials remained broadly unchanged overall – at over 55 per cent – and declined in Central Asia, the CEB region, eastern Europe and the Caucasus (EEC), and Russia (see Chart 14). The number of times that firms had been inspected by tax officials or required to meet them declined everywhere bar the CEB region (where it remained broadly unchanged), averaging just over two visits or meetings per year (see Chart 15). Several countries had also made it easier to pay tax by introducing electronic filing and payment systems or reducing the number of payments.ⁱⁱ All of these measures reduced tax officials' opportunities to seek informal payments. Indeed, with the exception of Bosnia and Herzegovina, Bulgaria, Kosovo, the Kyrgyz Republic, Lithuania, Montenegro and Ukraine, the percentage of firms reporting that informal payments were expected or requested either decreased or remained broadly unchanged relative to BEEPS IV.

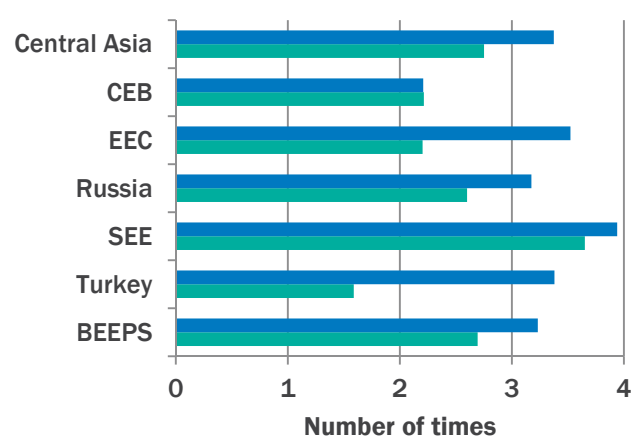
Chart 14. Firms visited or inspected by tax officials



■ BEEPS IV ■ BEEPS V

Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Chart 15. Number of times firms were inspected by or required to meet with tax officials



■ BEEPS IV ■ BEEPS V

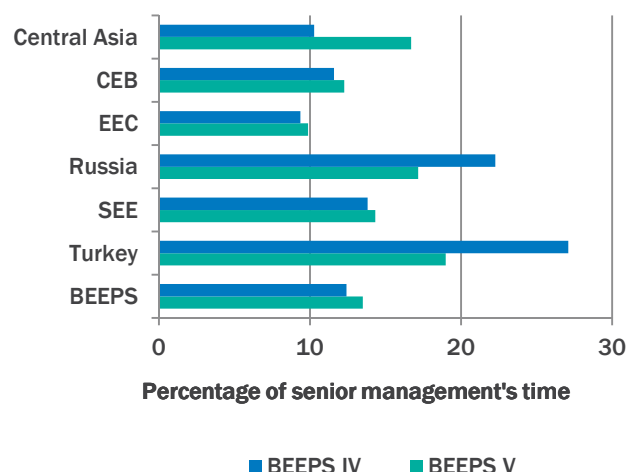
Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

It is more likely that the perceived severity of tax administration can be explained by “crisis taxes” and the unpredictability of countries’ tax regimes. Hungary, for example, introduced a sector-specific surtax in 2010 (abolished in 2013), which applied to the energy, retail and telecommunications sectors, while Poland increased social security contributions. Serbia increased many tax rates as part of the fiscal consolidation package that it adopted in 2012. The way that taxes are calculated and paid offers an alternative explanation. In most countries, firms are required to pay tax in advance on the basis of the tax paid or profits made in the previous year.

However, this did not take account of the fall in revenues owing to the global financial crisis.

Furthermore, the percentage of senior managers’ time that is spent dealing with requirements imposed by government regulations – such as taxes, customs, labour regulations, licensing and registration (including dealing with officials and completing forms) – increased by an average of around one percentage point, rising from 12.4 per cent in BEEPS IV to 13.5 per cent in BEEPS V (see Chart 16). The largest increases were recorded in Central Asia, while Russian and Turkish firms reported significant decreases.

Chart 16. Time spent dealing with government regulations



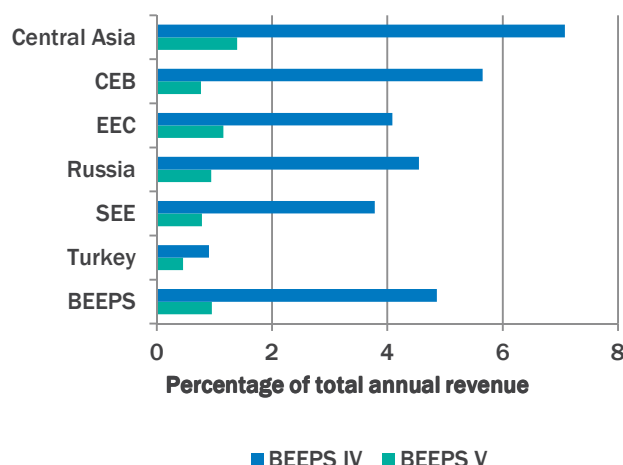
■ BEEPS IV ■ BEEPS V

Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Corruption

Corruption remains one of the main obstacles in transition countries, particularly for young firms. There is scope for corruption in any interaction that requires contact between firms and service providers or government officials. As discussed earlier, there was a slight increase in the share of firms reporting that informal payments were expected or requested when applying to be connected to electricity, but there was a decline in the share of firms reporting that informal payments were expected or requested by tax officials. Likewise, there was a decrease in the share of firms reporting that informal payments were expected or requested in order to obtain an import licence or an operating licence. There was an even larger decline in informal payments made to public officials to “get things done” with regard to customs, taxes, licences, regulations, services and the like, as well as an increase in the percentage of firms that reported never making such payments. In BEEPS V, firms reported that they paid out just under 1 per cent of their annual revenue for this purpose. In BEEPS IV, it was almost 5 per cent (see Chart 17). These positive developments can, to some extent, be explained by the introduction of electronic filing and payment systems in several countries, which reduces the amount of interaction between firms and officials and thereby reduces the opportunity and temptation to seek informal payments.

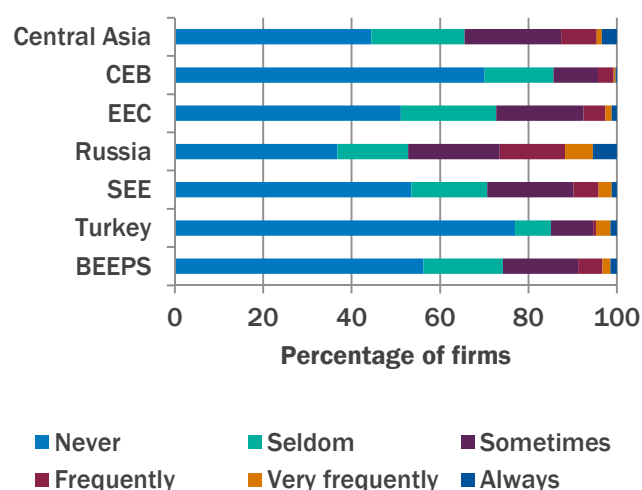
Chart 17. Informal payments to “get things done”



Source: BEEPS IV and V and author's calculations
Note: BEEPS IV was conducted in 2008-09. BEEPS V was conducted in 2013-14 (2011-12 in Russia)

The size of informal payments made to public officials to “get things done” decreased in all regions and in all countries. However, this type of corruption remained widespread in Russia and Central Asia, where less than 45 per cent of enterprises reported that they never made such payments (see Chart 18). Furthermore, in several countries the percentage of firms that made such payments at least occasionally increased relative to BEEPS IV – by more than 10 percentage points in Russia, Armenia and Lithuania.

Chart 18. Frequency of payments to public officials “to get things done”



Source: BEEPS V and author's calculations
Note: BEEPS V was conducted in 2013-14 (2011-12 in Russia)

Workforce skills

Workforce skills were among the top three obstacles in 11 of the 29 countries in BEEPS IV. In BEEPS V, however, this was the case in only 5 countries. The reason for this positive trend is not so much an improvement in education and training in the intervening period, but rather the global financial crisis, which affected the availability of skilled workers through three different channels: (i) reduced demand for skilled workers on the part of firms, which abandoned expansion plans or even shrunk; (ii) higher unemployment owing to firms laying off workers or going out of business, resulting in an increased supply of skilled workers; and (iii) fewer skilled workers moving abroad and/or more returning home, owing to economic conditions being worse abroad and/or better at home. Reliable data on immigration and emigration are hard to find, but the available information is at least indicative of general trends.

A case in point is Poland, where workforce skills were the second largest obstacle in BEEPS IV, a result of a significant number of Poles leaving the country after 2004. The Polish economy performed relatively well

during the global financial crisis, and many of those Poles returned. According to Eurostat data, the number of people moving to Poland was more than ten times the pre-crisis level during that period. As a result, workforce skills fell to eighth place in the list of obstacles in BEEPS V.

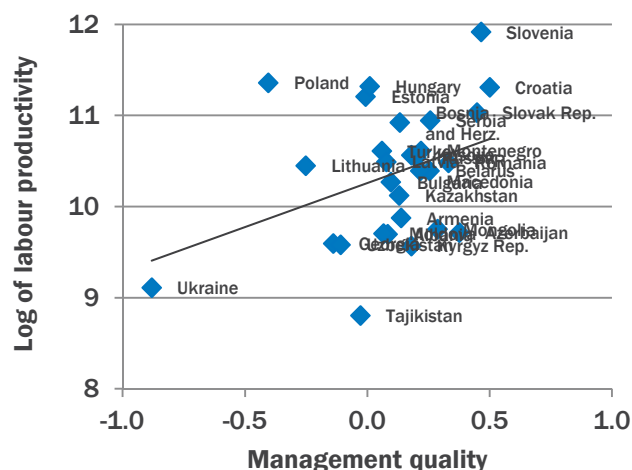
Romania's experience was similar – although not quite as dramatic – with workforce skills falling from third to fifth place. In 2010, 3 million Romanians (14.8% of the population) were estimated to be working abroad – mostly in Italy and Spain, which were hit hard by the crisis. This led to a significant reduction in the number of Romanians emigrating, as well as more Romanians returning home.

Workforce skills remained among the top three obstacles in the Baltic countries, Belarus and Moldova, which have experienced high levels of emigration in recent years. In the case of the Baltic countries, emigration – primarily to EU member states – increased after they joined the EU in 2004. In all of them, the number of people leaving dropped slightly in 2007. In Latvia and Lithuania, emigration then increased again as a result of the global financial crisis, which hit both countries hard. While emigration has decreased in recent years, it remains above pre-crisis levels. In Estonia, on the other hand, the number of people emigrating has continued to increase since 2007.

Management practices and innovation

There are other ways of improving firms' productivity, besides improving the external business environment. Firms' managers can make better use of excess capacity (if they have any), they can cut costs (shedding labour where necessary), and they can improve the way they manage their businesses. That is to say, firms themselves can improve how they handle production-related problems, monitor their production and set targets, as well as the way they deal with poor performers and reward high achievers. There is a strong correlation between the quality of management practices and firms' productivity (see Chart 19). In every country, there are firms with both good and bad management practices. A lack of managerial skills is one explanation for the low productivity of state-owned or state-controlled firms.

Chart 19. Average quality of management practices and average labour productivity

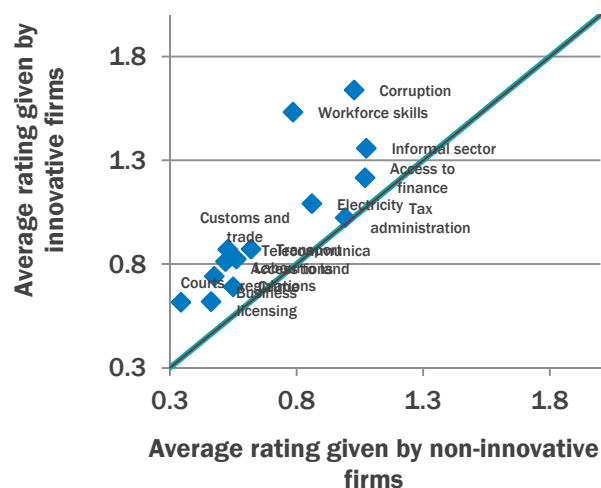


Source: BEEPS V and author's calculations

Note: BEEPS V was conducted in 2013-14 (2011-12 in Russia)

However, the most common and the most important driver of change within firms (particularly in advanced industrialised countries) is innovation, and the results of BEEPS V show that firms that have introduced a new product or process regard all aspects of their business environment as a greater constraint on their operations than firms that have not done so (see Chart 20). The differences between the views of innovative and non-innovative firms are especially large when it comes to workforce skills, corruption, and customs and trade regulations. Corruption is among the main constraints for all firms, and it is an even greater constraint for innovative firms. In contrast, customs and trade regulations are not major concerns at the level of the economy as a whole, partly because only a relatively small number of firms import production inputs or export their products directly. However, customs and trade regulations specifically affect innovative firms, as the introduction of new products and processes is often dependent on imported inputs and the ability to tap export markets.

Chart 20. Perception of the business environment: innovative versus non-innovative firms



Source: BEEPS V and author's calculations

Note: BEEPS V was conducted in 2013-14 (2011-12 in Russia).

Innovative firms are defined as firms that introduced new products or processes in the last three years.

Conclusion

Interviews with the managers of more than 15,500 firms across the transition region reveal that there has been only limited progress in regards to the main business environment constraints highlighted in the 2008-09 survey. Firms continue to complain first and foremost about informal competition from the shadow economy; their inability to access credit at reasonable terms; and problems related to accessing reliable and affordable electricity.

Since the 2008-09 round, firms have been considerably less constrained by the court system, business licensing and permits, and workforce skills. Improvements in courts and red tape were mainly the result of measures taken by various governments. FYR Macedonia, for example, revised most of its corporate governance in line with the European Union and international standards and equipped courts with electronic case management systems, which made the enforcement of contracts easier. Inadequate workforce skills, on the other hand, became a less severe obstacle due to increased return migration into the transition region in the wake of the global financial crisis.

ⁱ Respondents' answers may reflect differences in their "propensity to complain" – that is to say, differences in firms' sensitivity to constraints on their business – rather than actual differences in those constraints. For example, growing firms may regard workforce skills as more of an obstacle than shrinking firms, even if they are both in the same sector and location. In order to address this difficulty, this analysis uses the perceived severity of constraints to measure the quality of the various components of the business environment and controls for characteristics of individual firms (including size, age, industry and export activity), as well as characteristics of the individual manager who responded to the survey (such as gender, length of service and position within the firm).

ⁱⁱ According to Doing Business, Romanian firms have seen the average number of payments per year decrease from over 100 in 2008-09 to 39 in 2012-13 and 14 in 2013-14. Serbian firms still faced a total of 67 payments per year in 2013-14 (the highest figure in Europe).

The business environment in the transition region

The Business Environment and Enterprise Performance Survey (BEEPS), implemented by the EBRD in partnership with the World Bank Group, is a face-to-face survey with enterprise managers that examines the quality of the business environment.

Surveying the transition region

The fifth round of BEEPS was launched in Russia in August 2011, followed by other countries in late 2012 and early 2013. Fieldwork was completed in July 2014.

In total, top managers of more than 15,800 randomly selected firms were surveyed across 29 countries in which the EBRD works as well as the Czech Republic. Surveyed firms include small, medium and large enterprises in manufacturing, wholesale and retail trade, transport, construction and other service sectors.

The BEEPS covers topics such as infrastructure, competition, sale and supply, labour, innovation, land and permits, crime, finance and business-government relations. Firms were asked to express their opinions about the degree to which various components of the business environment represent obstacles to their current business operations, using a five-point scale: “no obstacle”, “minor”, “moderate”, “major” or “very severe obstacle”.

One difficulty in assessing the business environment lies in the fact that respondents' answers may reflect differences in the “propensity to complain”, that is, the sensitivity with which enterprises experience or report constraints on their business, rather than actual differences in these constraints. For example, growing firms may view workforce skills as more of an obstacle than shrinking enterprises, even if they are both in the same sector and location. In order to address this difficulty, the analysis uses the perceived severity of constraints as a measure of the quality of various components of the business environment and controls for the characteristics of the individual firm (including size, age, industry and export activity) as well as the characteristics of the manager who responded to the survey (gender, tenure and position within the firm). Because this type of analysis is based on the relative constraints as perceived by each firm, it can only indicate policy priorities and cannot be used to rank the countries by the quality of their business environment or to compare the severity of business environment obstacles across countries.

The BEEPS V results show that most firms in the transition region identified competitors' practices in the informal sector, (limited) access to finance and electricity issues as the main constraints. The reasons underlying this ranking vary across regions and countries. For example, in some countries enterprises complained about electricity because of the increase in industrial

energy prices, while others struggled with unpredictable electricity supply and experienced frequent power outages. For large firms (100+ employees), electricity ranked first place, followed by competitors' practices in the informal sector and access to finance. For firms less than 5 years old, on the other hand, access to finance was at the top, followed by competitors' practices in the informal sector and corruption. Access to finance was also the most binding constraint for manufacturing firms, while firms in the service sector put electricity at the top.

Cross-country variation




The business environment of course varies significantly across countries. The table below shows the three most binding constraints as perceived by representative firms in each of the 29 countries surveyed. In some countries, firms complain about elements of the business environment that do not, on average, rank highly as constraints in the transition region as a whole. For example, access to land was the third most binding constraint in Azerbaijan, but it does not feature among the top three in other countries.

There are some common business environment features across the regions, most noticeably so in south-eastern Europe, where competitors' practices in the informal sector were named as one of the three most binding constraints in six out of eight countries. In Central Asia, on the other hand, electricity issues were identified as one of the top three most binding constraints in all countries. It is also interesting to note that firms in labour-exporting countries such as Belarus, Latvia and Lithuania considered workforce skills to be the most binding obstacle.

The results also suggest that neighbouring countries often have very different profiles in terms of their business environment. For example, in the Kyrgyz Republic, firms perceived political instability, corruption and electricity issues to be the most important obstacles to their operations. By contrast, firms in neighbouring Tajikistan were most constrained by electricity issues, access to finance and competitors' practices in the informal sector.

The elements of the business environment that do not appear to be among the top three binding constraints in any of the transition countries are transport, crime, theft and disorder, labour regulations, telecommunications, customs and trade regulations, business licensing, and permits and courts. Customs and trade regulations were not seen as one of the top three constraints, which can be explained by the improved trade integration, with the European Union or the Eurasian Customs Union, as well as free trade agreements. The fact that courts were not regarded as a constraint is somewhat surprising, but is most likely the result of only a small percentage of firms in any given country going to court to settle disputes.

Business environment constraints		Informal sector	Access to finance	Electricity	Corruption	Political instability	Tax administration	Workforce skills	Transport	Crime	Labour regulations	Telecoms	Access to land	Customs & trade	Business licensing	Courts
Transition region																
Central Europe and the Baltic states	Croatia															
	Estonia															
	Hungary															
	Latvia															
	Lithuania															
	Poland															
	Slovak Republic															
	Slovenia															
South-eastern Europe	Albania															
	Bosnia and Herzegovina															
	Bulgaria															
	FYR Macedonia															
	Kosovo															
	Montenegro															
	Romania															
	Serbia															
Turkey																
Eastern Europe and the Caucasus	Armenia															
	Azerbaijan															
	Belarus															
	Georgia															
	Moldova															
	Ukraine															
Russia																
Central Asia	Kazakhstan															
	Kyrgyz Republic															
	Mongolia															
	Tajikistan															
	Uzbekistan															

 Highest score
  Second-highest score
  Third-highest score

Albania

In BEEPS V, the top three business environment obstacles identified by Albanian firms were electricity issues; competitors' practices in the informal sector; and corruption (Chart 1). Competitors' practices in the informal sector were the main obstacle for SMEs, while corruption was more problematic for large firms. Tax administration and access to land were among the chief constraints for young firms.

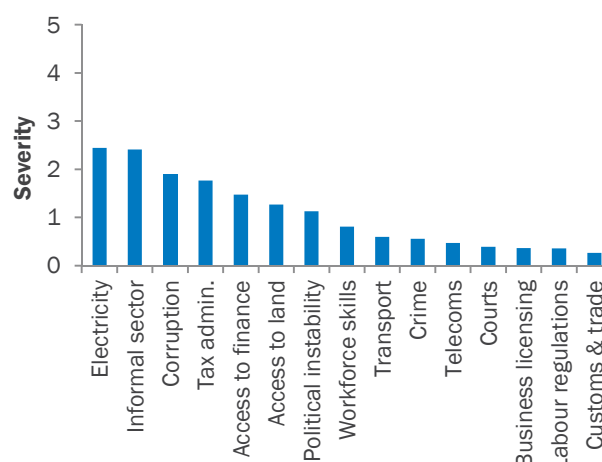
Improvements in reliability of electricity supply and concerns about corruption

Though some improvements have taken place since BEEPS IV, **electricity issues** remained the most severe obstacle for firms in Albania. The number of power outages in a typical month decreased from 32.8 in 2007 to 7.8 in the latest BEEPS round, partly owing to increased precipitation. However, this still exceeded the south-eastern Europe (SEE) average of 5.4. The percentage of annual revenue lost due to power outages decreased from 15% in 2007 to 7.7% in the latest survey (Chart 2).

The **informal sector** has been a major issue in Albania since the early stages of its transition towards a market economy. In BEEPS V, 40.2% of the firms surveyed reported competing against firms in the informal sector, which is slightly below the SEE average of 48.6%. This competition is highest among SMEs: 41% of them reported competing against unregistered firms, compared with 27.8% of large firms. The informal sector is an important contributor to employment and production in Albania. According to the International Labour Organization, 30% of the total workforce in the construction sector is employed informally. Discrepancies in Albania's national accounts suggest that the informal sector accounted on average for 36.2% of GDP over the period 1996-2012. This leads to tax revenue losses, a lack of labour protection and unfair competition among firms.

Corruption replaced political instability as the third most important obstacle in BEEPS V. Although relatively few firms applied for construction-related permits, almost one-third of the firms that did said that an informal gift or payment was expected or requested during the application process, well above the SEE average of 18.8%. Likewise, although informal payments typically made by firms to secure a government contract dropped from 6.5% (of contract value) in BEEPS IV to 1.5% in BEEPS V, it was above the SEE average of 1% (Chart 3). Similarly, the percentage of firms that never had to make informal payments to "get things done" increased to 52.7%, but was still slightly below the average of 56.2% for transition countries.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Losses due to power outages

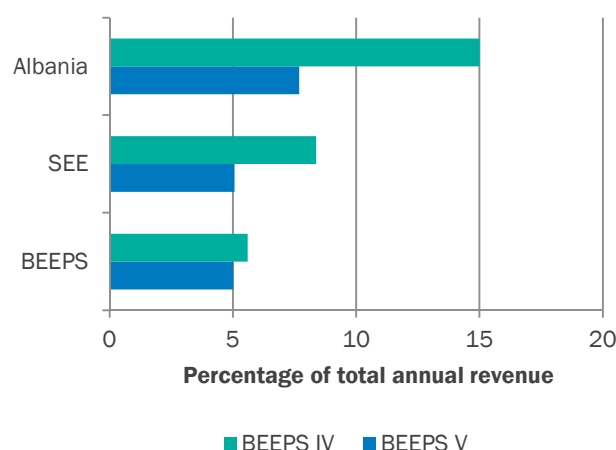
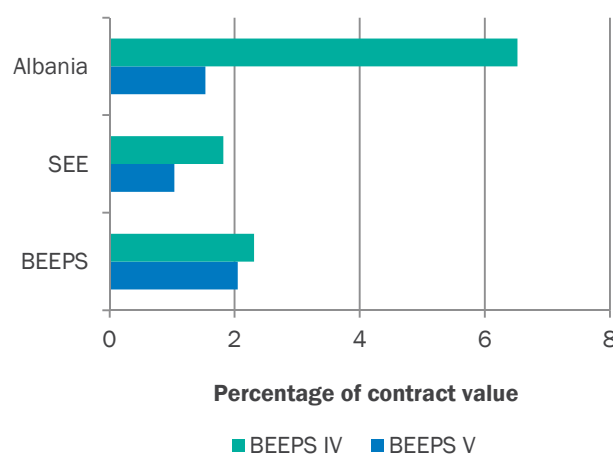


Chart 3. Informal payments to secure a government contract



Armenia

In BEEPS V, the top three business environment obstacles identified by Armenian firms were access to finance; tax administration; and political instability (Chart 1). Young firms complained heavily about customs and trade regulations. In BEEPS IV, political instability, access to finance and the informal sector were the top obstacles.

Reliance on bank lending and inefficient customs regulations

Access to finance emerged as the main constraint for Armenian firms. While the value of required collateral increased substantially, from 60% in BEEPS IV to over 200% in BEEPS V, this disproportionately affected SMEs and young firms, which were also more credit-constrained than large and old firms. Compared with their counterparts in eastern Europe and the Caucasus (EEC), Armenian firms depended less on internal funds to finance working capital, and instead relied on bank loans and other sources, such as moneylenders, friends and relatives. Just over a quarter of firms purchased fixed assets (compared with more than a half in BEEPS IV), and almost three-quarters of such purchases were financed using internal funds (compared with less than a half in BEEPS IV). Bank financing decreased from 21.7% to 9.5% and was below the EEC average, while other sources of financing were higher in Armenia than in other EEC countries (Chart 2).

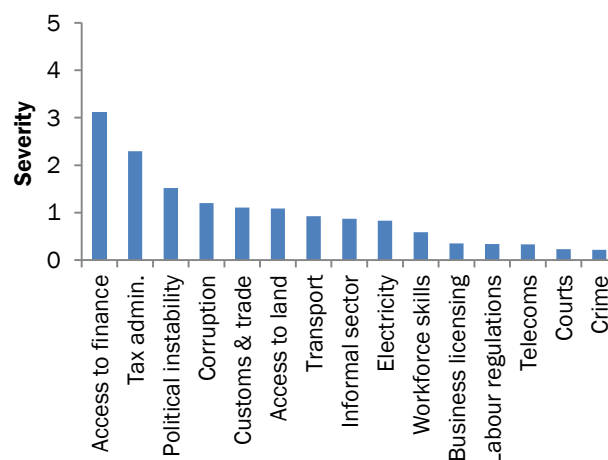
Roughly three-quarters of firms were visited or inspected by tax officials in both rounds of BEEPS – nearly 18 percentage points above the EEC average in the latest round. This, together with the tendency of tax officers to impose at least one fine per visit even if no violation had been committed, could explain why **tax administration** emerged as the second biggest obstacle. However, the frequency of inspections by tax officials and the percentage of firms being asked for informal gifts or payments decreased since BEEPS IV. Inspections were more common among large firms – almost all of them were inspected – but tax officials were more likely to expect or request an informal payment from SMEs.

Political instability was the third major constraint. The unresolved conflict in Nagorno-Karabakh sustains a possible threat of military escalation and thus deters investment. In addition, the economic blockade imposed by Azerbaijan and Turkey, again due to unresolved conflict, increases costs for businesses. Firms may also be concerned about frequent amendments in policy and legislation.

It's not surprising to see **customs and trade regulations** amid the top obstacles for Armenian firms. On average, it took 8.6 days to clear customs for direct exports and 17.6 days for direct imports. Both figures exceeded the EEC and BEEPS V averages (Chart 3). This is particularly worrying given that Armenia is a small open economy whose business sector relies heavily on trade.

Survey fieldwork period: November 2012 – July 2013. EEC: Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine. Small and medium-sized enterprises (SMEs) have 5-99 employees. Young firms are less than 5 years old.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Sources of financing of fixed asset purchases

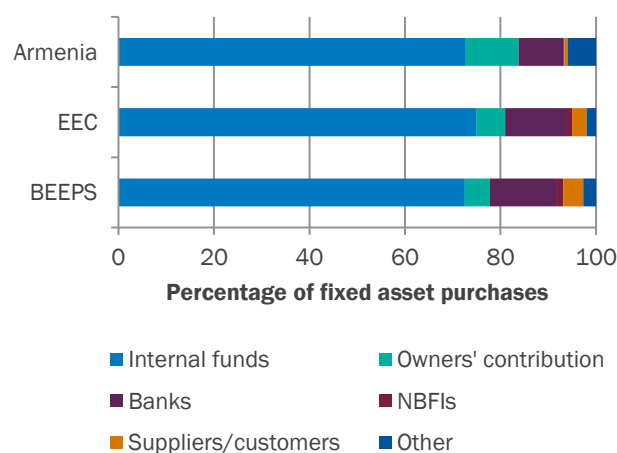
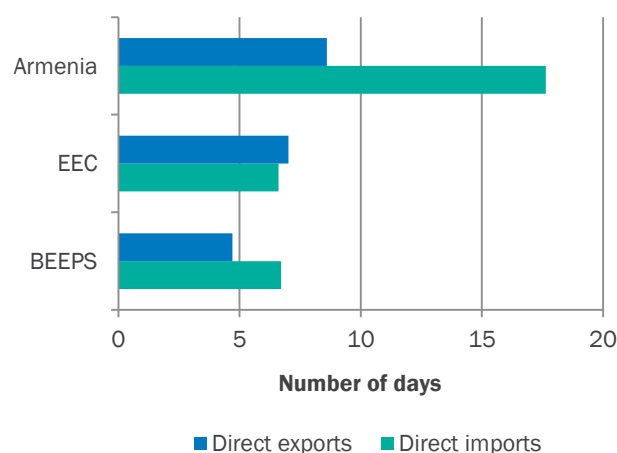


Chart 3. Customs clearance for direct exports and imports



Azerbaijan

In BEEPS V, the top three business environment obstacles identified by Azerbaijani firms were competitors' practices in the informal sector; access to finance; and access to land (Chart 1). Access to finance was the main constraint for young firms and firms in the service sector. In BEEPS IV, corruption replaced access to finance as one of the top obstacles.

Very limited access to finance, but some success in tackling corruption

The share of firms that compete against unregistered or informal firms decreased significantly from 40.7% to 18.4%, possibly due to measures introduced in 2009 aimed at making it easier to start a business.

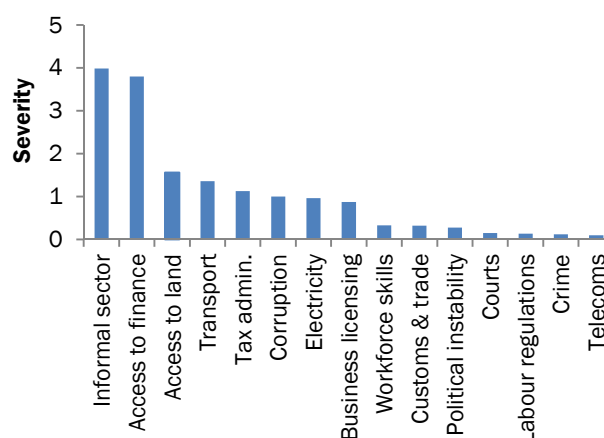
Nonetheless, **competitors' practices in the informal sector** emerged as the top obstacle in BEEPS V.

Access to finance was one of the biggest problems in Azerbaijan. Very few Azerbaijani firms relied on loans to finance their operational activities. Only 14.6% of firms had a loan or a line of credit, down from 19.9% in BEEPS IV, representing the lowest share among BEEPS countries (Chart 2). Working capital was predominantly financed through internal funds (92.8%, highest among BEEPS countries), while bank financing accounted for only 4.7%. Of all firms surveyed, 18.6% reported that their owner used outstanding personal loans to finance their business activities, which is above the eastern Europe and the Caucasus (EEC) average of 14.1%. More than 65% of firms that needed a loan were either discouraged from applying for a loan or rejected when they did, which is above the EEC average of 53.3%.

Access to land remained in third place, despite a significant reduction in the waiting time for a construction-related permit (from 46.5 to 13.7 days) and a sharp drop in the share of firms reporting that an informal payment was expected or requested in relation to that permit – from 54.7% in BEEPS IV to 8.2% in BEEPS V. However, it is proximity to the capital and land quality that matter. The demolition of old buildings in Baku to clear paths for luxury real estate projects may have reduced the availability of land and driven up prices for many firms.

Azerbaijan turned out to be quite successful in tackling **corruption**. The government was recently praised by the Organisation for Economic Co-operation and Development for its anti-corruption measures, including the adoption of new legislation and the success of the Prosecutor General's Anti-Corruption Department. This is also reflected in BEEPS, as fewer firms reported that an informal payment was expected or requested when meeting with tax officials and when applying for electrical connections and construction-related permits.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Firms with a loan or a credit line

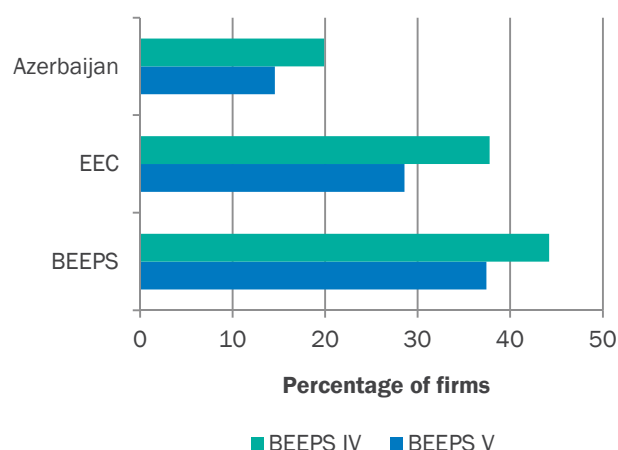
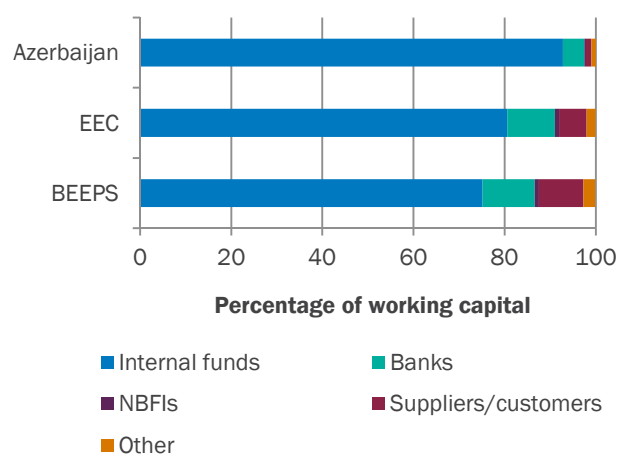


Chart 3. Sources of financing of working capital



Belarus

In BEEPS V, the top three obstacles identified by firms in Belarus were workforce skills; access to finance; and competitors' practices in the informal sector (Chart 1). Large and manufacturing firms found access to land particularly difficult, while firms in the service sector were hampered by electricity-related issues. Workforce skills and electricity are persistent obstacles as they also topped the list in BEEPS IV.

Migration of qualified workforce and reliance on internal funds

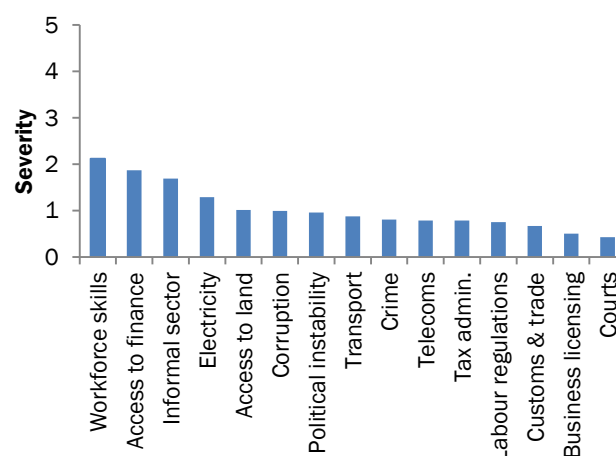
Inadequate workforce skills remained the biggest obstacle faced by Belarusian firms. The country continued to suffer from a drain of qualified workforce, mainly into Russia, especially after the liberalisation of labour migration within the Common Economic Space in 2012. With average wages in Belarus being 40% below those in Russia in 2013, this phenomenon is not surprising. Even more important are the wage differentials across qualifications, which are very narrow (only 50% of returns in Russia), limiting the returns to investment in education and training. However, following the recent devaluation of the Russian rouble, the outflow of highly skilled workers to Russia has somewhat slowed.

Regarding **access to finance**, the share of Belarusian firms with a loan or a credit line declined significantly from almost 50% in BEEPS IV to 30.4% in BEEPS V. Firms also faced on average shorter loan durations than their counterparts in eastern Europe and the Caucasus (EEC): 26.6 months compared with 29.7 months. Of the 60.5% of firms who needed a loan, 41.6% were credit-constrained; most of them were discouraged from applying for a loan due to high interest rates. SMEs and young firms were the most affected by the lack of bank financing: 45% of SMEs and 60.9% of young firms that needed a loan were credit-constrained, compared with 16.3% of large and 36.3% of old firms.

In line with the downward trend in EEC, the prevalence of **competition with the informal sector** in Belarus has become less of a concern since the previous BEEPS round. Of the firms surveyed, 50.4% reported competing against firms in the informal sector in BEEPS IV compared with 42.8% in BEEPS V (Chart 2).

Belarus inherited one of the highest standards of scientific and technical potential in the former Soviet Union. This is reflected in the share of innovative firms: new processes were introduced by 21.7% of firms, while 18.1% of firms introduced new products. Both shares were well above the BEEPS averages of 8.9% and 10.8%, respectively. Belarus has several well-known innovative companies, such as Polimaster (radiation detection equipment) and Izovac (thin film coating technologies for touch screens).

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

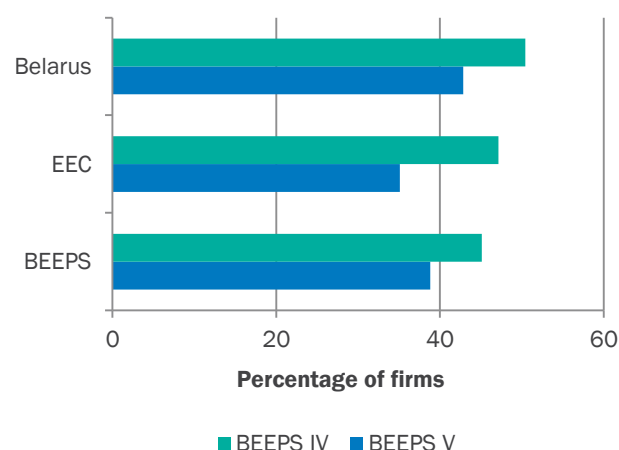
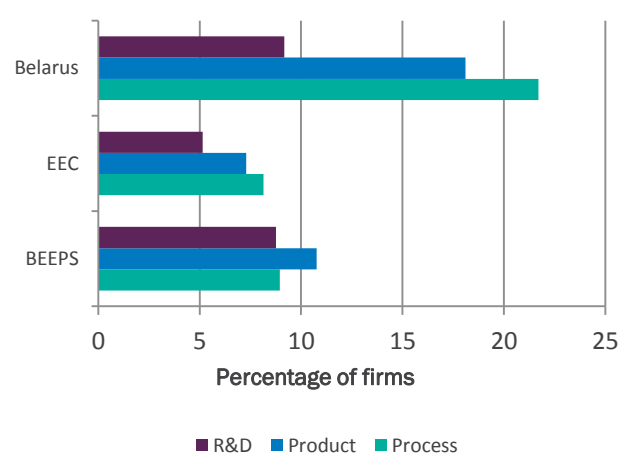


Chart 3. Engagement in innovation activities



Bosnia and Herzegovina

In BEEPS V, the top three business environment obstacles identified by firms in Bosnia and Herzegovina were political instability; access to finance; and competitors' practices in the informal sector (Chart 1). SMEs ranked the practices of the informal sector above access to finance, while electricity issues were in third place for large firms. Access to finance and corruption were the main constraints for young firms, while old firms were concerned about corruption. In BEEPS IV, the top two obstacles were the same, with tax administration taking third place.

Relatively good access to loans, but increasing corruption

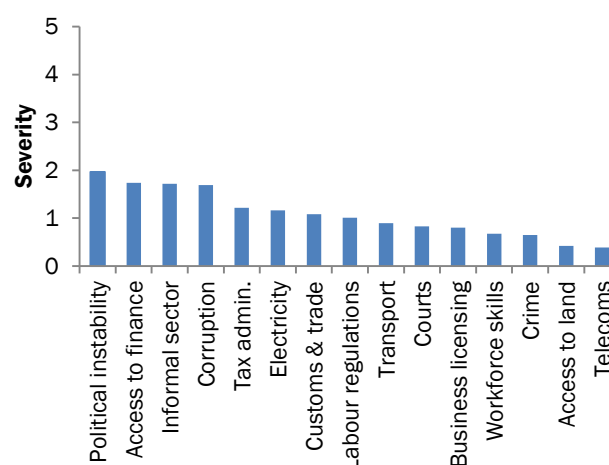
Bosnia and Herzegovina's complex administrative, political and legal framework, established after the devastating war in 1992-95, makes it one of the most corruption-prone states in Europe according to several sources. The country itself is not politically unstable, but political rigidity as a result of the war may explain why **political instability** was rated as the top obstacle.

Though some of the firms in Bosnia and Herzegovina complained about **access to finance**, many of them had reasonably good access, at least to bank loans, compared with the rest of the countries in south-eastern Europe (SEE). In financing their working capital and fixed asset purchases, firms relied predominantly on bank borrowing and credit purchases. In fact, Bosnia and Herzegovina was among the top three SEE countries with the highest share of firms that had a line of credit or a loan. Of the firms surveyed, 66.3% had a loan or a credit line – around 17 percentage points higher than the SEE average. However, the median amount of collateral required increased from 150% to 200% of the loan value and remained above the SEE average of 172% (Chart 2).

Competitors' practices in the informal sector were, as in most other SEE countries, among the top three obstacles. Of the firms surveyed, 44% reported competing with unregistered firms or firms in the informal sector.

Corruption remained an important issue in Bosnia and Herzegovina. The percentage of firms that were asked for informal payments by tax officials increased from 1.4% in BEEPS IV to 6.5% in BEEPS V, the second highest in the SEE region. The percentage of firms reporting that informal payments were expected or requested to obtain an operating licence increased from 6% to almost 14%, well above the SEE average of 5.8% (Chart 3). Transparency International reported that the anti-corruption agency had not yet started carrying out any activities as of January 2013, although its management was appointed in 2011.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Median collateral required

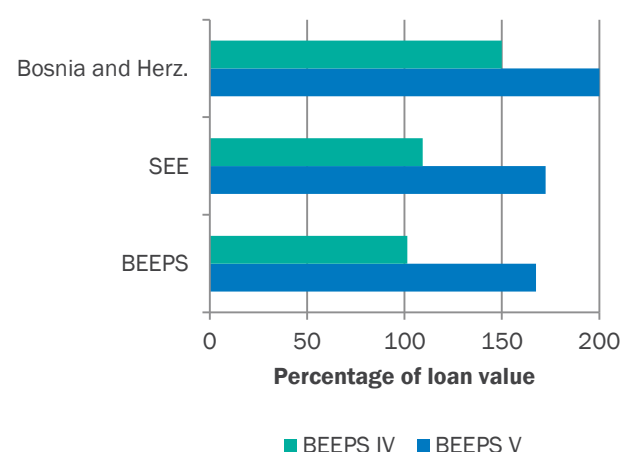
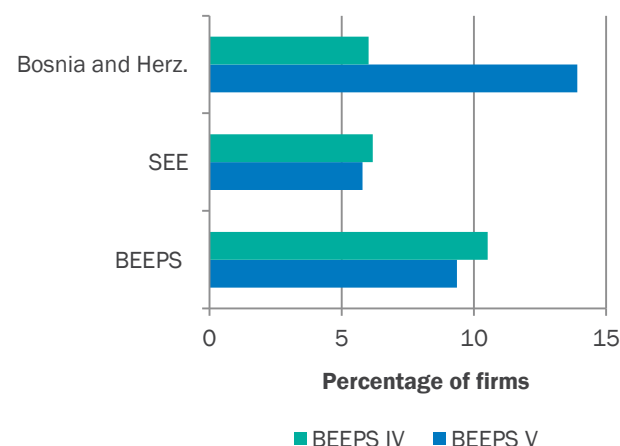


Chart 3. Informal payments to obtain an operating licence



Bulgaria

In BEEPS V, the top three business environment obstacles identified by Bulgarian firms were competitors' practices in the informal sector; political instability; and corruption (Chart 1). Large firms also complained about labour regulations, while young firms were concerned about transport, competitors' practices in the informal sector and workforce skills. Since BEEPS IV, access to finance and electricity issues have become relatively less problematic.

Shadow economy and continued corruption concerns

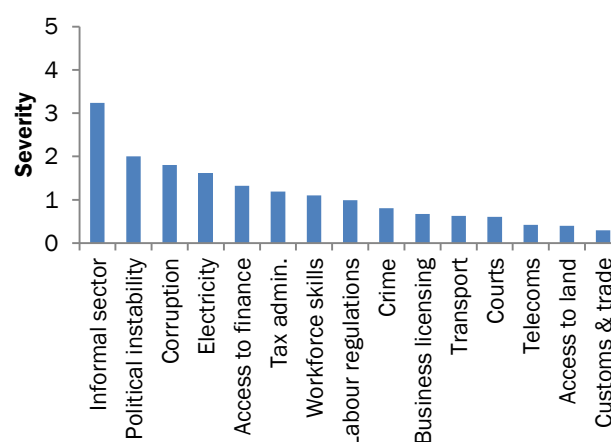
Competitors' practices in the informal sector remained a major issue. The share of firms that competed against unregistered or informal firms increased from 54.1% in BEEPS IV to almost 60% in BEEPS V (Chart 2). Analysis by the World Bank suggests that the problem lies in the lack of economic viability for low-wage earners in the formal sector. Single persons who earn less than the minimum wage in the informal sector would have to give up 50% to 70% of their income to formalise.

Electricity issues remained among the top three obstacles mentioned by manufacturing firms. Corporate users are able to choose a supplier, but the state's involvement in regulation, electricity generation and transmission continues to inhibit the development of open price competition. Moreover, the public has lost confidence in the management of energy companies and the government's oversight of the electricity sector. Top concerns included the time needed to obtain an electrical connection – on average 49.6 days or 13 days longer than the BEEPS V average (Chart 3) – and informal payments for electrical connections. Of the firms surveyed, 28% reported that an informal payment was expected or requested, by far the highest share in south-eastern Europe (SEE).

In fact, concerns about electricity billing practices led to demonstrations in winter 2012, which eventually led to the government resigning in February 2013, followed by early elections in May 2013. The weak coalition survived a second wave of protests against controversial political appointments; however, the new government was unable to avoid another round of early elections in late 2014. Frequent changes in government since February 2013 most likely explain why **political instability** was identified as the second most severe obstacle in 2012-13.

Corruption was the third main constraint. In BEEPS V, almost 60% of firms reported making informal payments to "get things done" at least once in a while. The level was higher than the 55% reported in BEEPS IV and more than 16 percentage points above the BEEPS V average. However, firms considered corruption to be more of a solution than a problem, which is disconcerting.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

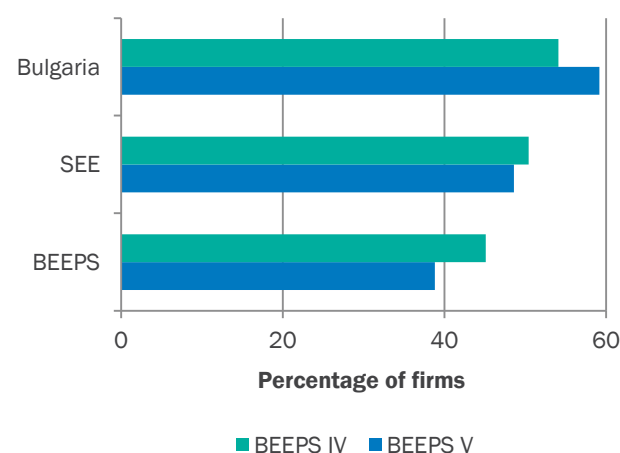
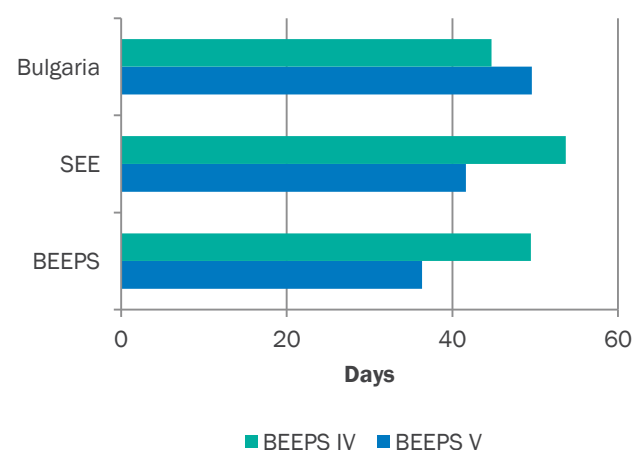


Chart 3. Waiting time to be connected to electricity



Croatia

In BEEPS V, the top three business environment obstacles identified by Croatian firms were access to finance; competitors' practices in the informal sector; and tax administration (Chart 1). The same obstacles were also ranked at the top in BEEPS IV, pointing to little improvement in these areas. Large firms found tax administration to be their biggest struggle, followed by access to finance and labour regulations, while manufacturing firms ranked corruption as the second main constraint.

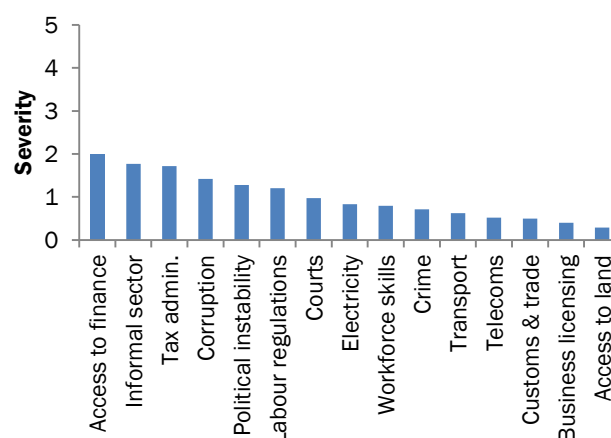
Access to finance emerges as the top business environment obstacle

Access to finance emerged as the top obstacle in Croatia. Of the firms surveyed, 29% applied for a loan or a line of credit in BEEPS V and almost 30% of them reported that their application was rejected; nearly double the central Europe and the Baltic states (CEB) average. Of those that did not apply for a loan, 17.3% stated that the reason was high interest rates (Chart 2). Of the firms surveyed, 53.7% had a credit line or a loan, which is above the CEB average of 40.5%. However, more than half of the firms (55.1%) that needed a loan were credit-constrained – they were either discouraged from applying for a loan or rejected when they applied. Croatian firms relied more on bank financing than CEB firms on average: around 18.6% of fixed assets and 9.8% of working capital were financed by bank loans, and the median collateral (as a percentage of loan value) was 173%, well above the CEB median of 153%. In regard to payment, 56.6% of purchases and 61.5% of sales were paid after delivery in BEEPS V, compared with around 51.5% for both in CEB.

In the latest BEEPS round, 48% of firms reported that they **competed against unregistered or informal firms** – the second highest in CEB after Lithuania. This is a very high percentage, as the CEB average is only 35%, and could be a consequence of the state's relatively strict labour regulations. Croatia has focused on repressive measures to tackle undeclared work, but has made little use of incentives to encourage those working in the informal sector to formalise. Measures to foster commitment to tax morality are also fairly recent.

Tax administration was also a major concern. In BEEPS V senior management spent 22.7% (compared with 16% in BEEPS IV) of their time dealing with government regulations, almost twice the CEB average of 11.6% (Chart 3). Of the firms surveyed, 35% were inspected by tax officials in BEEPS V, slightly below the CEB average of 36%. The frequency of inspections by tax officials has not changed significantly since BEEPS IV; it remained at roughly three visits per year.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Reasons for not applying for a loan

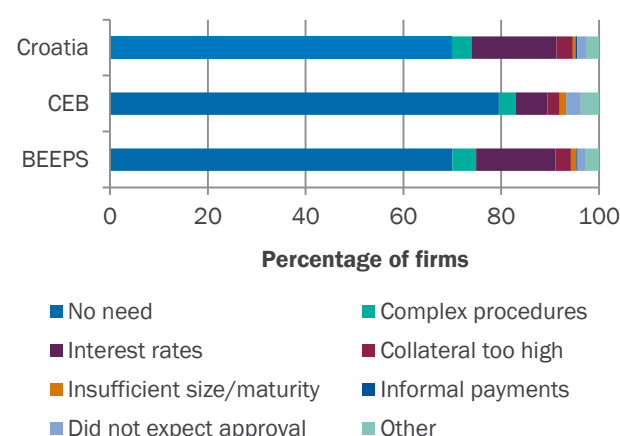
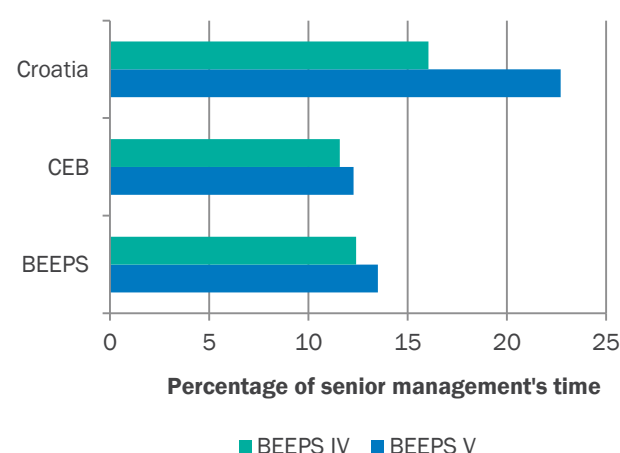


Chart 3. Dealing with government regulations



Estonia

In BEEPS V, the top three business environment obstacles identified by Estonian firms were competitors' practices in the informal sector; electricity issues; and workforce skills (Chart 1). Large firms felt most constrained by workforce skills, while young firms complained about electricity issues, tax rates and transport. In BEEPS IV, the top three obstacles were workforce skills, political instability and labour regulations.

More firms competing with firms in the informal sector; labour market mismatches

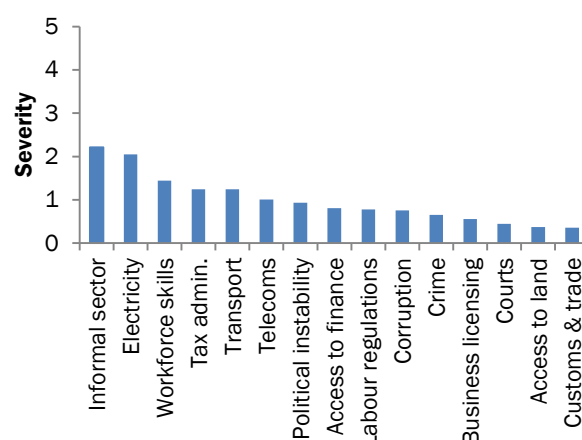
The share of firms that **compete against firms in the informal sector** increased from 26.3% in BEEPS IV to 35.7% in BEEPS V, making it almost equal to the central Europe and the Baltic states (CEB) average of 35% (Chart 2).

When it comes to **electricity**, Estonia performed better than the regional average. In BEEPS V only 1.1% of sales were lost due to power outages compared with a CEB average of 2.3%. The number of power cuts in a typical month was around 1.9 and 1.8 in BEEPS IV and V, respectively. However, electricity issues were ranked as the second biggest obstacle. This could be linked to an increase in electricity prices during the period in which the survey was conducted. Although electricity prices in Estonia are among the cheapest in the European Union, they increased by 22% between the second half of 2012 and the second half of 2013. Electricity prices fell again as a result of the completion of the new electricity link (EstLink2) in early 2014.

Workforce skills continued to be among the top three obstacles. One of the main reasons for this concern is that young and well-educated Estonians are migrating to western European countries that offer better career opportunities. According to the Estonian Population and Housing Census, emigration has reduced the country's population number by 6,629 people (0.5% of the total population). Another reason is the existence of labour market mismatches. The existence of such mismatches is a sign that human capital is not being utilised in the most efficient way. As of 2014, 8.4% of Estonia's youth (under the age of 31) are considered to be over-educated (that is, their current level of schooling is higher than the required level to perform the job).

Tax administration was also one of the top concerns in the country. On average, the number of inspections by, or meetings with, tax officials increased from 2 to 2.8 – above the regional average of 2.2 and the second highest in the CEB region after Croatia (Chart 3).

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

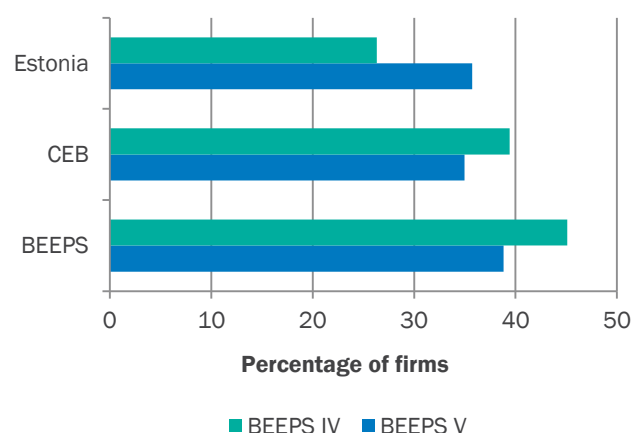
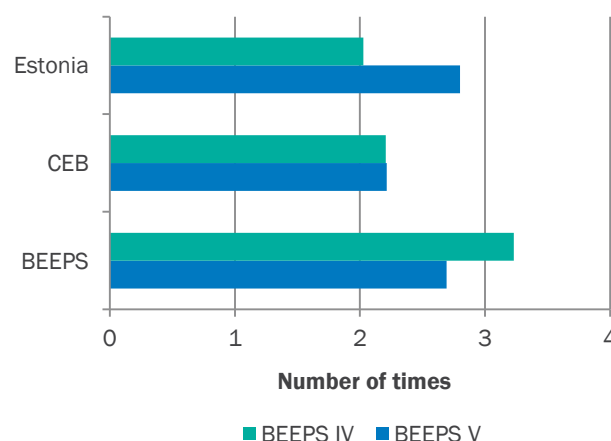


Chart 3. Tax official inspections/meetings



FYR Macedonia

In BEEPS V, the top three business environment obstacles identified by FYR Macedonian firms were competitors' practices in the informal sector; access to finance; and electricity issues (Chart 1). Electricity issues, transport and competitors' practices in the informal sector were most problematic for large firms, while young firms also complained about tax administration. Electricity issues were more pressing than access to finance for old firms, manufacturing companies and firms in the service sector. In BEEPS IV, political instability was in third place.

Heavy reliance on internal funds and retained earnings; successful judicial reforms

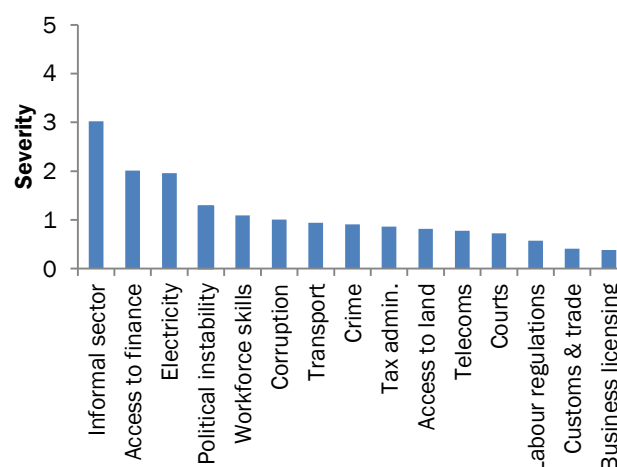
Although there have been some improvements in dealing with unregistered firms, **competitors' practices in the informal sector** remained the biggest problem for FYR Macedonian firms. The percentage of firms that reported competing against firms in the informal sector decreased from 74% in BEEPS IV to 56% in BEEPS V. However, it still exceeded the south-eastern Europe (SEE) average by almost 7 percentage points, putting FYR Macedonia in third place among SEE countries (Chart 2).

Access to finance has always been one of the top obstacles for FYR Macedonian firms. In financing their working capital and fixed assets, they relied heavily on internal funds and retained earnings: in BEEPS V, 81% of fixed asset purchases (up from 60.6% in BEEPS IV) and 78% of working capital was financed through internal funds rather than banks or other financial institutions (Chart 3). The share of credit-constrained firms remained about the same as in BEEPS IV, at 56%. Access to finance was relatively more limited for SMEs than large firms.

Analysis by the International Monetary Fund points to the inefficiency of **electricity** use, limited options for electricity supply and ageing generation facilities as the main challenges for the country's electricity sector. The share of revenue lost due to power cuts decreased from 11.8% in BEEPS IV to 7.5% in BEEPS V, but was still very high compared with the BEEPS V average and was the second highest in SEE, topped only by Kosovo.

There have been improvements in the **court** system, as indicated by its low ranking as an obstacle, moving from 4th to 12th place. Most of the corporate governance legislation has recently been revised in line with European Union and international standards. The share of firms that agree or strongly agree that the court system is fair, quick and able to enforce its decisions significantly increased and stood at 61%, 47% and 66%, respectively. The respective shares in BEEPS IV were much lower at 32%, 19% and 37%.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

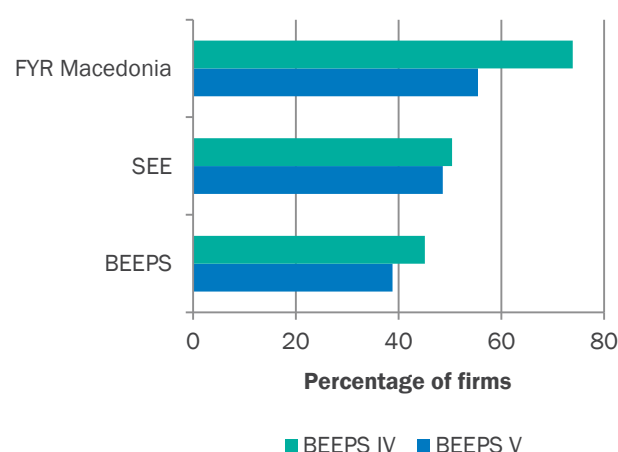
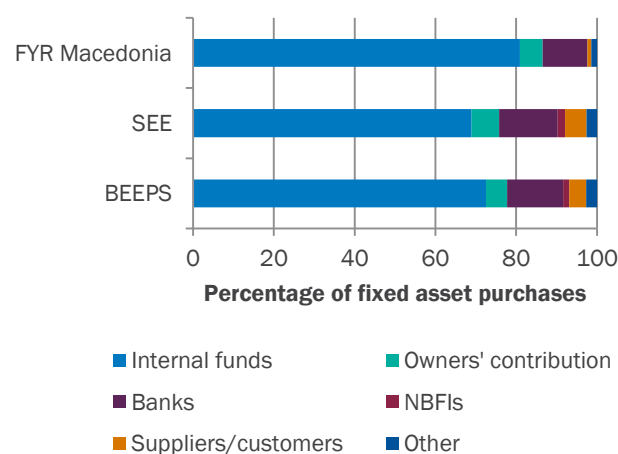


Chart 3. Sources of financing of fixed asset purchases



Georgia

In BEEPS V, the top three obstacles in the business environment identified by Georgian firms were political instability; electricity issues; and access to finance (Chart 1). SMEs and young, old and manufacturing firms were somewhat more concerned about competitors' practices in the informal sector than access to finance. The main obstacles have not changed since BEEPS IV.

Electricity concerns on the rise

Georgia has experienced high levels of **political instability** since the collapse of the Soviet Union, particularly during the 1990s. The October 2012 parliamentary elections and the October 2013 presidential elections were the first occasions since independence in 1991 on which power had been transferred to the opposition through a peaceful democratic election. Georgia is often plagued by squabbles between the new and outgoing governments.

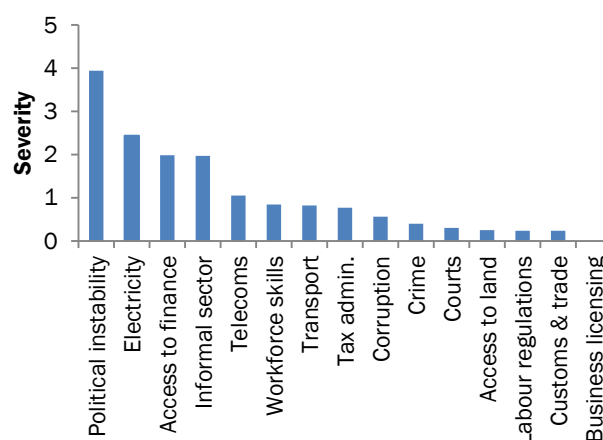
Electricity issues were the second most severe constraint named by Georgian firms. Although fewer firms experienced power outages – 26.1% in BEEPS V, compared with 41.4% in BEEPS IV – and they were shorter in duration on average, losses due to power cuts increased from 5% to 9% of total annual revenue, almost double the eastern Europe and the Caucasus (EEC) average of 4.8% (Chart 2). The main problem Georgia faces is related to the security of electricity supply: the large hydro power plants are in disputed areas or in areas close to disputed territories.

Access to finance was in third place. Almost 36% of the firms surveyed had a loan or a credit line (slightly below the BEEPS V average of 37.4%). The financial sector suffered a slow-down in the first half of 2013 due to business deleveraging and political uncertainty. More than 40% of loans to SMEs were in US dollars, while large enterprises financed themselves predominantly in local currency. This poses significant currency risks for those SMEs, especially non-exporters, that are not naturally hedged against exchange rate fluctuations.

Just over half – 54% – of Georgian firms reported to **compete against firms in the informal sector** in BEEPS V, exceeding the EEC average by roughly 20 percentage points (Chart 3). This share is the highest in EEC and has increased since BEEPS IV. For a number of years the World Bank's *Doing Business* report has ranked Georgia among the top performers in terms of ease of starting a business, so this finding indicates that other regulations matter as well.

Crime, theft and disorder moved from 6th place in BEEPS IV to 10th place in BEEPS V. The share of firms that experienced losses as a result of theft, robbery, vandalism or arson on their premises decreased substantially since BEEPS IV, and the losses were less than a third of those they experienced then: 2.2% of total annual revenue in BEEPS V compared with 7.6% in BEEPS IV.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Losses due to power outages

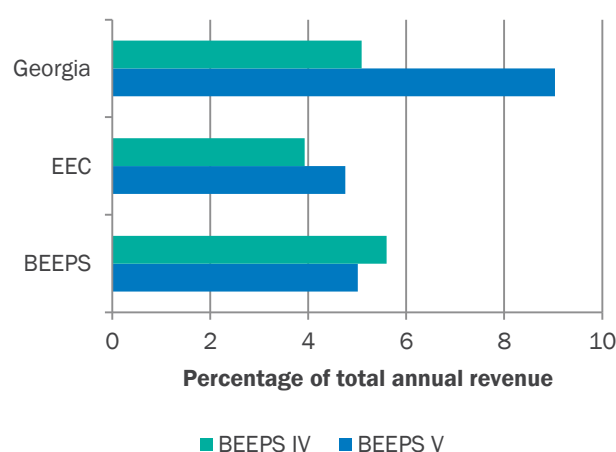
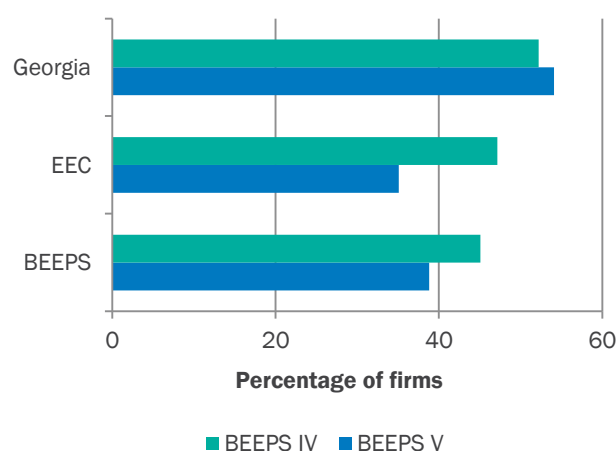


Chart 3. Competition from the informal sector



Hungary

In BEEPS V, the top three obstacles in the business environment that Hungarian firms identified were tax administration; political instability; and competitors' practices in the informal sector (Chart 1). The most severe constraints for large firms were competitors' practices in the informal sector, labour regulations and electricity issues. Transport, telecommunications and electricity issues topped the list for young firms.

An unpredictable tax regime

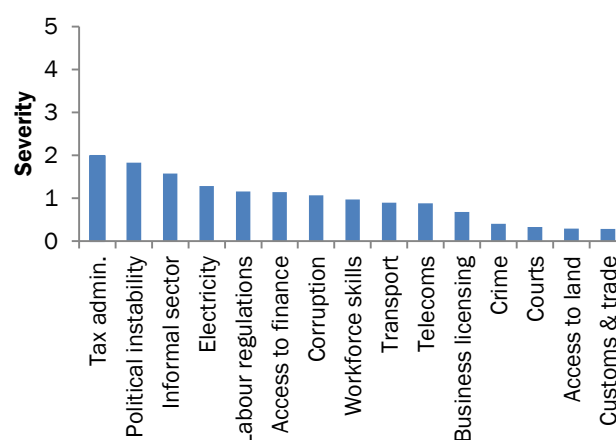
Tax administration became the top obstacle to doing business. The share of firms visited by tax officials increased from 49.8% in BEEPS IV to 56% in BEEPS V, 20 percentage points higher than the central Europe and the Baltic states (CEB) average (Chart 2). The number of times firms were inspected by tax officials also increased: from 1.8 in BEEPS IV to 2.2 in BEEPS V. Foreign firms expressed displeasure with the unpredictability of Hungary's tax regime, the retroactive nature of some of the tax measures, and the volume and speed with which the government was introducing new economic measures and changes. Senior management spent 12.8% of its time dealing with government regulations, slightly above the CEB average of 12.3%.

Political instability may have emerged as one of the top obstacles due to: high levels of budget deficit; the legal uncertainty for businesses resulting from major political reforms launched by the dominant majority government in 2012-13 (over 700 new laws were adopted along with a new constitution); and the government's propensity to use its political majority to target banks with taxes and other costs without sufficient consultation.

Competitors' practices in the informal sector remained among the top three obstacles. According to the European Commission and the International Labour Organization, the size of the shadow economy as a percentage of GDP in Hungary is 22.5%, which is above the EU average of 14.9%. Nevertheless, the share of firms that reported to compete against firms in the informal sector decreased from 49% in BEEPS IV to 13% in BEEPS V, the lowest share in CEB. This improvement may be because of reforms to the process of starting a business – such as online registration – introduced since the previous BEEPS round.

Electricity issues were the fourth major obstacle faced by Hungarian firms. Although the number of power outages in a typical month halved compared with BEEPS IV, the percentage of surveyed firms experiencing them increased from 16.6% to 20.5% in BEEPS V. The losses due to power outages increased from 1.2% of total annual revenue to 5.2% in BEEPS V (Chart 3). This percentage was the highest among countries in CEB, where the average was 2.3%.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Visited or inspected by tax officials

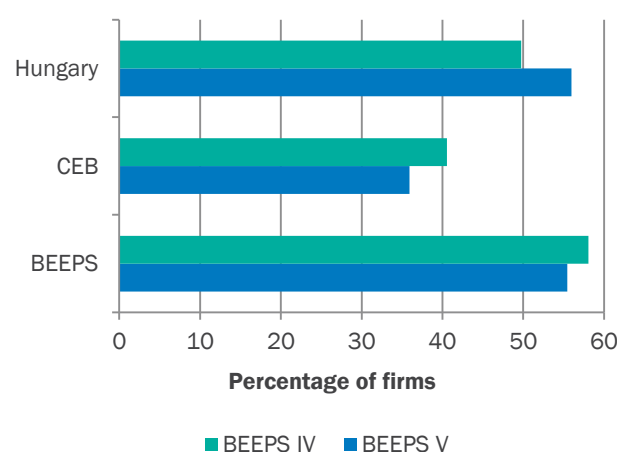
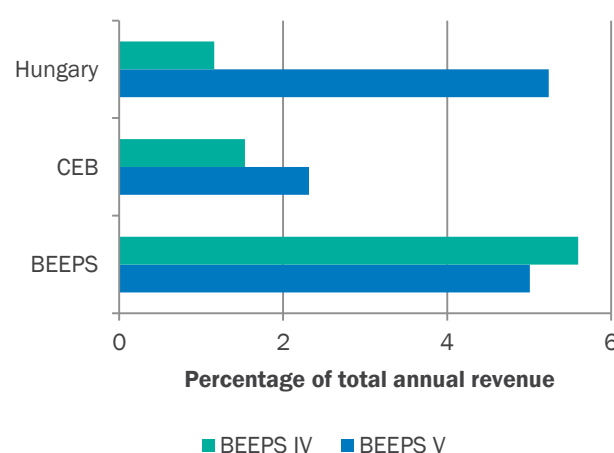


Chart 3. Losses due to power outages



Kazakhstan

In BEEPS V, the top three business environment obstacles identified by firms in Kazakhstan were competitors' practices in the informal sector; electricity issues; and access to finance (Chart 1). For large firms, electricity issues and workforce skills were among the biggest challenges. Young firms listed corruption as a major constraint. In BEEPS IV, the top three obstacles were workforce skills, access to finance and electricity issues.

Limited access to finance, skilled workers and electricity remain a challenge

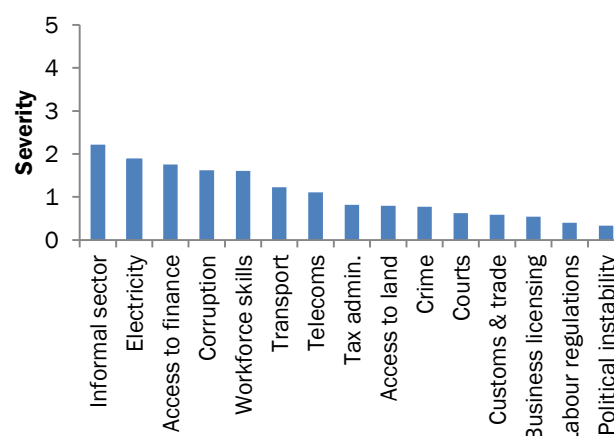
Competitors' practices in the informal sector emerged as the biggest challenge in the business environment in Kazakhstan in BEEPS V. In contrast to some of the other countries in Central Asia (CA), the share of firms competing against unregistered firms decreased by only 2 percentage points since BEEPS IV, to 34.7%.

Electricity issues remained in second place, despite many improvements since BEEPS IV. The average number of days to obtain an electrical connection decreased from 102 to 32, the duration of power outages halved and the losses resulting from power outages decreased from 5.4% of total annual revenue in BEEPS IV to 3.8% in BEEPS V. However, the share of firms that reported an informal payment was expected or requested to obtain an electricity connection increased to 33% and exceeded the BEEPS average by 21 percentage points (Chart 2).

With regard to **access to finance**, only 19.2% of all establishments had a loan or a line of credit in BEEPS V, down from 33.2% in BEEPS IV (Chart 3). The share of bank financing of fixed asset purchases decreased from 17.7% in BEEPS IV to 8.8% in BEEPS V, below both the CA and BEEPS averages. The collateral requirements for loans more than doubled to the median of 170% of loan value. The share of firms that applied for a loan in BEEPS V – at 15.4% – was roughly half of that in BEEPS IV, and almost a third of them were rejected, all of them SMEs (amounting to 37% of SMEs that applied for a loan). The share of firms that needed a loan but were discouraged from applying increased from 46.8% in BEEPS IV to almost 60% in BEEPS V.

Workforce skills were less binding than in BEEPS IV, moving from first to fifth place. The percentage of employees with a university degree increased from 33.8% in BEEPS IV to 44%, which was higher than the CA average and about 14 percentage points higher than the BEEPS average. Part of this effect might be due to the reduction in migrant labour quotas imposed by the Kazakh government in response to the financial crisis.

Chart 1. Business environment obstacles

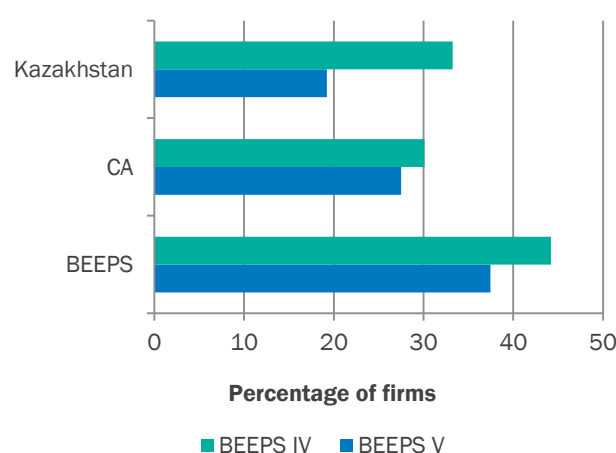


Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Informal payments to obtain electricity



Chart 3. Firms with a loan or a credit line



Kosovo

In BEEPS V, the top three business environment obstacles identified by Kosovan firms were competitors' practices in the informal sector; electricity issues; and corruption (Chart 1). SMEs placed corruption ahead of electricity issues, while electricity issues; access to finance; and crime, theft and disorder topped the list for large firms. Crime, theft and disorder were also a concern for young firms. In BEEPS IV, crime, theft and disorder replaced competitors' practices in the informal sector to appear among the biggest challenges in the business environment.

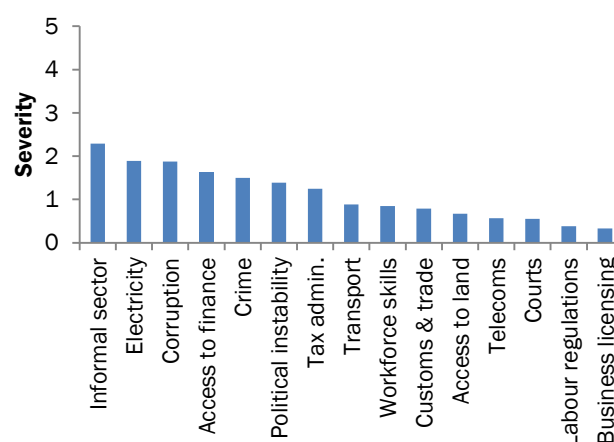
Competition from the informal sector intensifies and corruption is a major concern

It is not surprising that **competitors' practices in the informal sector** appeared as the major obstacle to business in Kosovo. The share of firms that reported competing against firms in the informal sector amounted to 66% and was the highest among all the 30 countries covered in the survey (average of 39%); almost all SMEs operate informally – at least in part. Moreover, almost no progress has been seen in tackling informal sector competition since BEEPS IV when the share of firms that competed against informal sector firms was 64% (Chart 2).

Electricity issues were much worse in Kosovo than in most other transition countries and posed a huge problem for Kosovan firms in their day-to-day business. Most of them suffered from frequent power outages. In BEEPS V, 81% of Kosovan firms – the highest share among the countries covered – experienced on average 13.6 power outages per month. While this was a significant improvement on BEEPS IV, in terms of the share of firms experiencing outages and their frequency, both of these indicators were the worst in south-eastern Europe (SEE), where firms experienced on average 5.4 power outages per month. Frequency was second only to Uzbekistan. Firms also bore the highest losses from power outages in SEE – 11.3% of total annual revenue (Chart 3).

Corruption remained among the top three obstacles: the percentage of contract value typically paid to secure a government contract increased from 1% in BEEPS IV to 4.3% in BEEPS V. The share of firms asked to make an informal payment to obtain a construction-related permit increased from 0.7% to 9.6% in BEEPS V. In addition, the share of firms that were asked for informal payments by tax officials was 9.5% in BEEPS V, above the SEE average of 6.3%. Moreover, firms were perceived to spend 2.2% of total annual revenue on informal payments or gifts, almost four times the SEE average of 0.8%.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

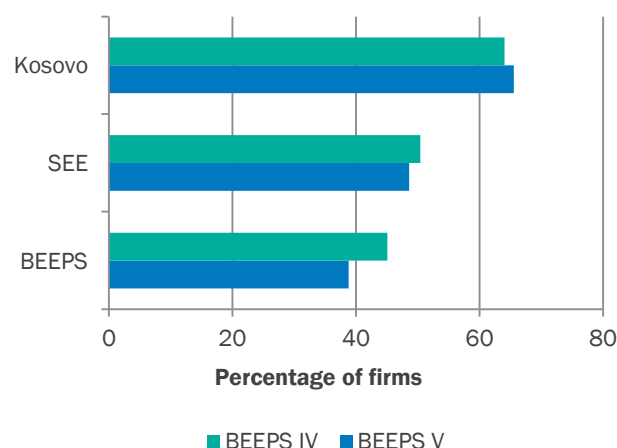
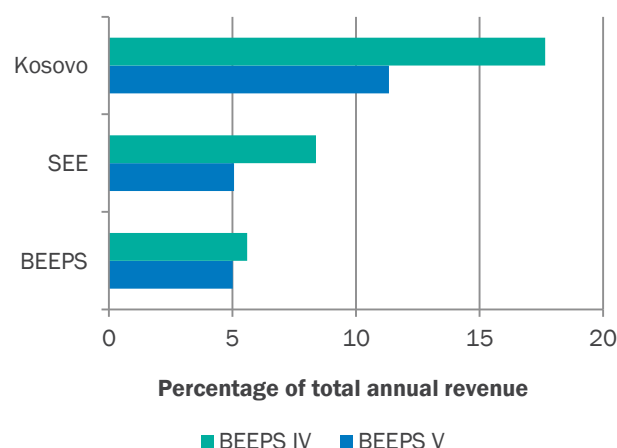


Chart 3. Losses due to power outages



Kyrgyz Republic

In BEEPS V, the top three business environment obstacles identified by Kyrgyz firms were political instability; corruption; and electricity issues (Chart 1). Large and manufacturing firms felt more constrained by competitors' practices in the informal sector. In BEEPS IV, competitors' practices in the informal sector were among the most binding business environment constraints, instead of political instability.

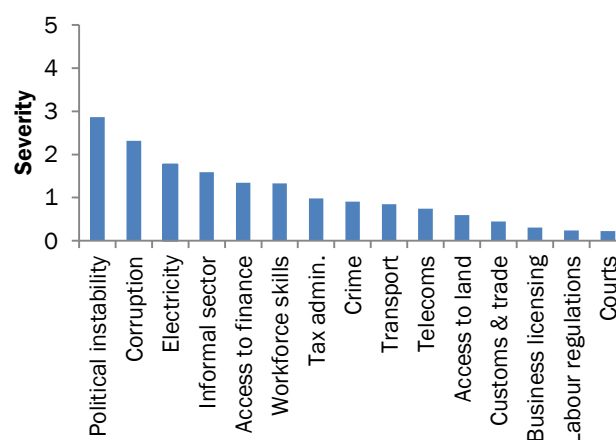
Corruption continues to be a challenge, electricity issues improve

Political instability was identified as a major obstacle for Kyrgyz firms. The political and social instability of 2010-11 led to a change of government following widespread public demonstrations. The country emerged from a period of political upheaval with a more democratically oriented political system and a reform-minded government.

Corruption has always been one of the major obstacles for Kyrgyz firms. However, concerns about corruption rose dramatically in BEEPS V. A significantly higher share of firms reported that an informal payment was expected or requested when obtaining an electrical connection (50%, up from 37.3%), an import licence (65.5%, up from 23.2%), an operating licence (58%, up from 22.6%) or when dealing with tax administration (53%, up from 35.9%). Only in the case of construction-related permits did this share decline, from 55.8% to 43.1% (Chart 2). Moreover, in 4 out of 5 named cases this share was the highest among the 30 surveyed countries, except for construction-related permits. With 2.9% of contract value, the Kyrgyz Republic was also among the leaders in the value of informal payments made by enterprises to secure government contracts. There was a silver lining, however: firms in the Kyrgyz Republic viewed corruption as more of a problem than a solution.

Since BEEPS IV there were some improvements in the area of **electricity**, which was no longer the biggest obstacle. While the wait for an electrical connection more than doubled, from 25 days to almost 55 days, and the share of firms that experienced power outages in BEEPS V increased to 72.9% (the third highest among the surveyed countries, after Kosovo and Montenegro), the frequency and duration of outages decreased substantially. In BEEPS IV, an average firm in the Kyrgyz Republic would experience 6.7 outages in a typical month, lasting 7.4 hours each. In BEEPS V, it would experience 1.6 outages per month, lasting 3.7 hours each. The losses from power outages also plummeted from 13.7% to 5.6% of total annual revenue (Chart 3). Overall, SMEs experienced greater losses from power outages than large firms.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Informal payments expected or requested

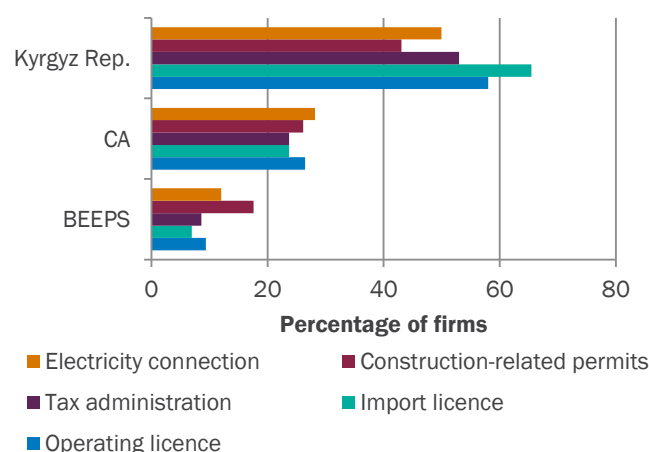
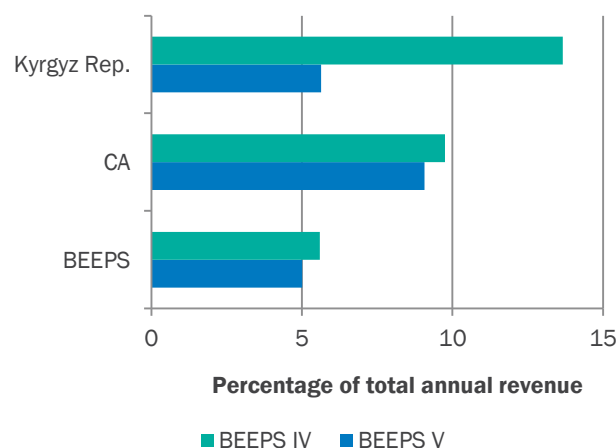


Chart 3. Losses due to power outages



Latvia

In BEEPS V, the top three business environment obstacles identified by Latvian firms were workforce skills; access to finance; and political instability (Chart 1). SMEs and young firms were mostly concerned about access to finance, while large and manufacturing firms were constrained by electricity issues. Young firms were also affected by competitors' practices in the informal sector. In BEEPS IV tax administration, rather than access to finance, was among the top three business environment obstacles.

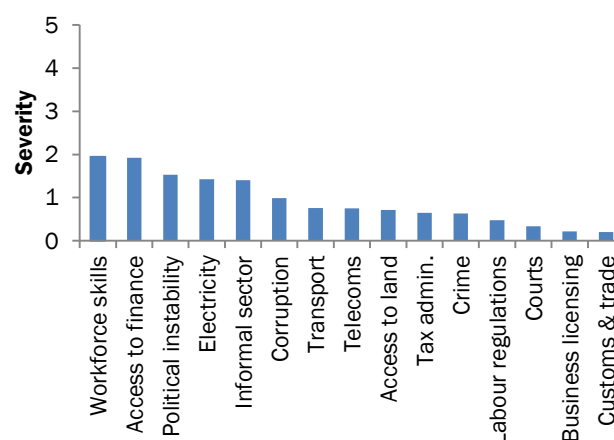
Workforce skills remain a challenge and access to finance is a constraint

Latvian firms identified **workforce skills** as the top obstacle. In 2004, when the country first joined the EU, most of the emigrant workers were moderately educated individuals from rural areas, where unemployment rates are the highest. However, the number of emigrants, and the human capital they take with them, has increased over the years. Young and highly educated workers now tend to migrate to western Europe in search of better career opportunities. This is a concern for Latvia, as it is a country with an ageing and shrinking population. As of 2012, around 80% of the emigrants are under 35.

When it comes to **access to finance**, the share of bank loans used to finance fixed assets has decreased in all countries in central Europe and the Baltic states (CEB). The reduction was particularly striking in Latvia, where the share in BEEPS V was less than a quarter of the share in BEEPS IV and less than half of the average share in CEB (Chart 2). Only around 6% of fixed assets were financed through bank loans, compared with a CEB average of almost 16%. The share of firms with a loan or a credit line more than halved too, from 48.5% in BEEPS IV to 20.1% in BEEPS V, which is below the CEB average of 40.5% (Chart 3). However, only 26.9% of firms reported needing a bank loan and just over half of those (52.5%) turned out to be credit-constrained – they either did not apply for a loan (despite needing it) or were rejected by the bank when they did. Among young firms, only 15.1% reported needing a bank loan, but more than 80% of them were credit-constrained. The share of credit-constrained large firms almost doubled from 23.3% in BEEPS IV to over 45% in BEEPS V.

Political instability was perceived to be the third most severe obstacle to Latvian firms. In 2011 parliament was dissolved following a corruption scandal. The relationship between businesses and politics, combined with low levels of trust in parliamentary and political institutions, has posed problems in Latvia since the country regained its independence in 1991.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Sources of financing of fixed asset purchases

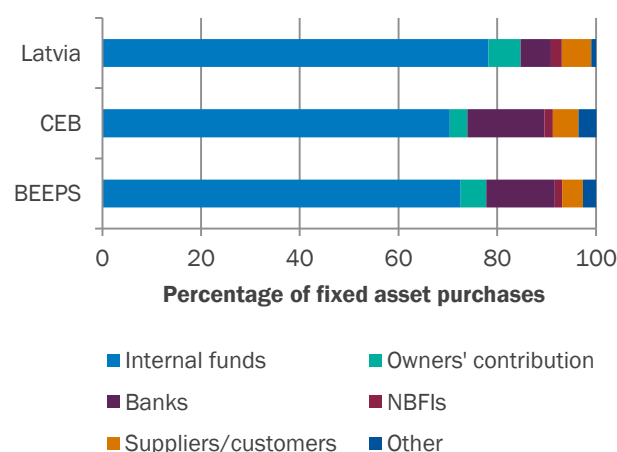
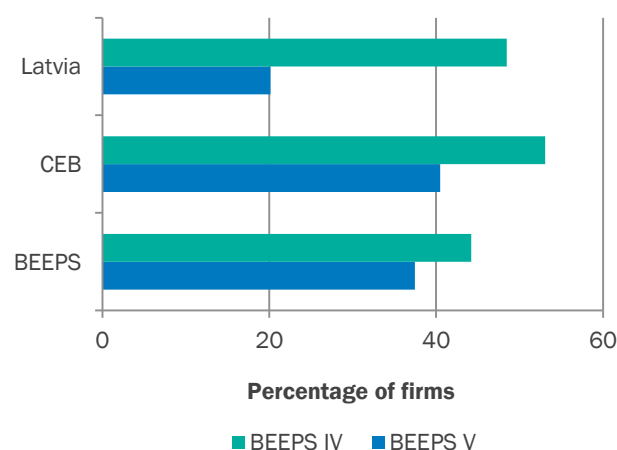


Chart 3. Firms with a loan or a credit line



Lithuania

In BEEPS V, the three largest obstacles in the business environment, as identified by Lithuanian firms, were workforce skills; competitors' practices in the informal sector; and electricity issues (Chart 1). Corruption was one of the most binding constraints for large and young firms, while manufacturing firms cited limited access to finance. In BEEPS IV political instability; workforce skills; and electricity issues were considered the three major business environment obstacles, while competitors' practices in the informal sector ranked eighth.

Workforce skills remain the most severe business environment constraint

The concern regarding the **skills of the workforce** stems from the fact that many educated young people are emigrating to find better work opportunities. According to Reuters, Lithuania has the highest level of migration in the EU. In 2010, 83,000 people (2.6% of the population) left the country, followed by almost 54,000 in 2011. Between 2002 and 2012 the outward mobility of Lithuanian students doubled.

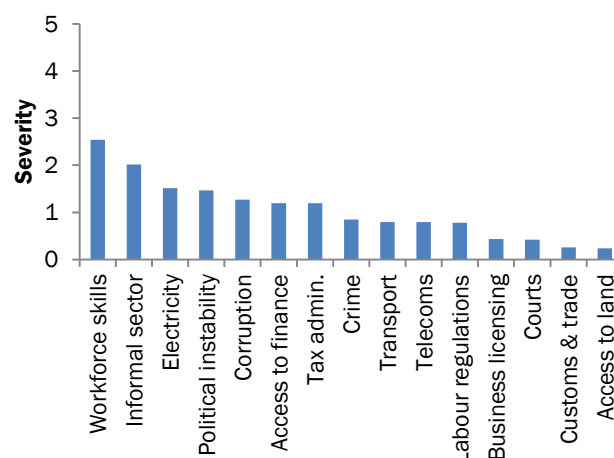
Of the firms surveyed, 58% reported that they had been **competing against unregistered or informal firms** (Chart 2). This was the highest share among countries in central Europe and the Baltic states (CEB). It is also above the average of countries covered in the survey (39%).

Electricity issues remained in third place, despite a favourable comparison with other countries in CEB on many indicators. The duration of power outages was 1.8 days compared with a CEB average of 3 days. On average, power outages occurred 2.4 times in a month compared with the CEB average of 2.3. Only 0.9% of total annual revenue was lost due to power outages compared with a CEB average of 2.3%. The reason behind the firms' concerns is likely to be linked to electricity prices. In 2012 the price of electricity in Lithuania was €0.114 per kilowatt hour (kWh), which was above the EU average of €0.094 per kWh.

As in all EU countries that experienced both financial and budget deficit crises, **political instability** emerged as one of the largest obstacles in Lithuania in BEEPS IV. In BEEPS V, the situation had improved and political instability moved down from first to fourth place.

Corruption remained an issue. The share of firms reporting that informal payments were expected or requested when applying for an electrical connection almost quadrupled since the previous round, increasing from 2.7% to 10.1%, which makes it the highest in the region (Chart 3). Moreover, the share of firms reporting that they had never made informal payments "to get things done" decreased from 72.7% to 62.4%.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

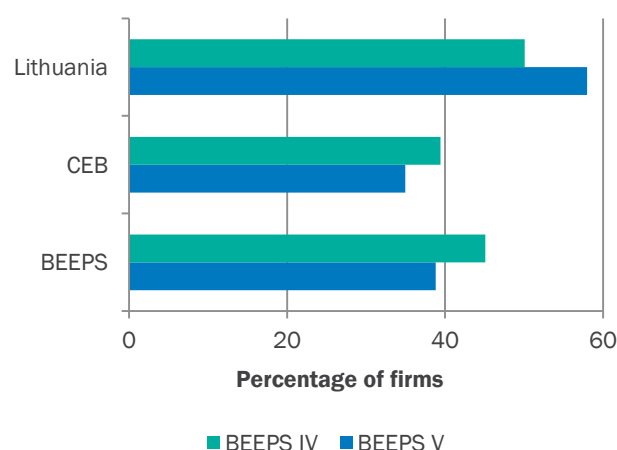
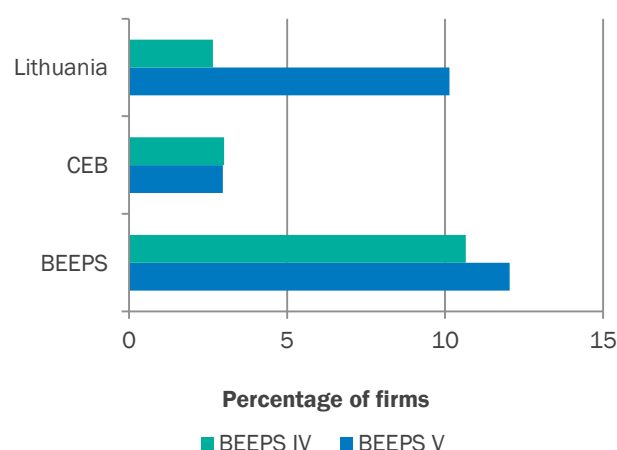


Chart 3. Informal payments to be connected to electricity



Moldova

In BEEPS V, the three largest business environment obstacles identified by Moldovan firms were corruption; political instability; and workforce skills (Chart 1). Large firms also felt constrained by electricity issues, while young firms placed labour regulations among the biggest obstacles. In BEEPS IV, access to land; workforce skills; and access to finance were the three major constraints.

Higher prevalence of corruption and continued concerns about workforce skills

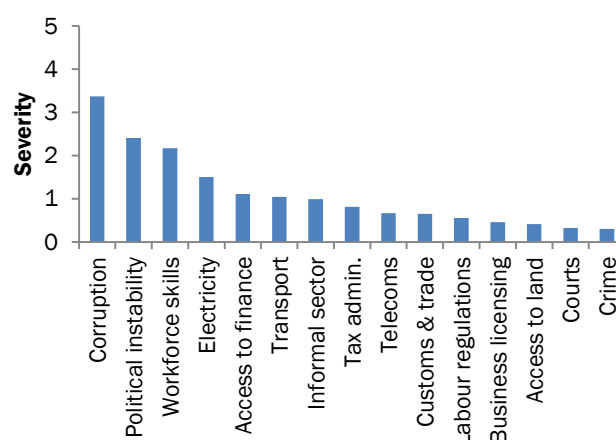
Since BEEPS IV the relative severity of **corruption** for Moldovan firms has significantly increased, moving from eighth place in BEEPS IV to first place in BEEPS V. Moldovan firms were much more likely to report that an informal payment was expected or requested than an average firm in eastern Europe and the Caucasus (EEC) region. The share of firms reporting that an informal payment was expected or requested in relation to applications for various items has increased significantly since BEEPS IV: for an electrical connection from 1.6% to 23% (Chart 2); for a construction-related permit from 22.8% to 42.4%; for an import licence from 5.9% to 8.6%; and for an operating licence from 6.9% to 22%. There have been some improvements, too: the share of firms reporting that informal payments were expected or requested in meetings with tax officials decreased from 14.2% to 12.4%, and the informal payments made by firms to public officials to “get things done” dropped from 2.9% to 0.2% of total annual sales.

Political instability due to the fragility of the ruling coalitions has been a major concern in Moldova since April 2009, preventing the country from passing judicial reforms. However, there have been some positive developments since the general elections in 2012 in the areas of freedom of the media, the police and education.

Lack of skilled workers is a point of concern for firms. Since nearly 285,000 of Moldovan migrants live in Russia (about 8% of the total population), 170,000 in Ukraine and 90,000 in Italy, it is not surprising that firms complain about the lack of educated and **skilled workforce**. Indeed, in Moldovan firms the share of full-time employees with a completed university degree was substantially lower than the EEC average – 30.1% versus 45.8% (Chart 3). Large firms have notably lower shares of university graduates among their full-time employees than SMEs.

There have been improvements in **access to land**, as indicated by its low ranking as an obstacle, moving from first to 13th place. Since BEEPS IV, Moldova made registering property easier and less time consuming by eliminating the requirement for cadastral sketches.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Informal payments to be connected to electricity

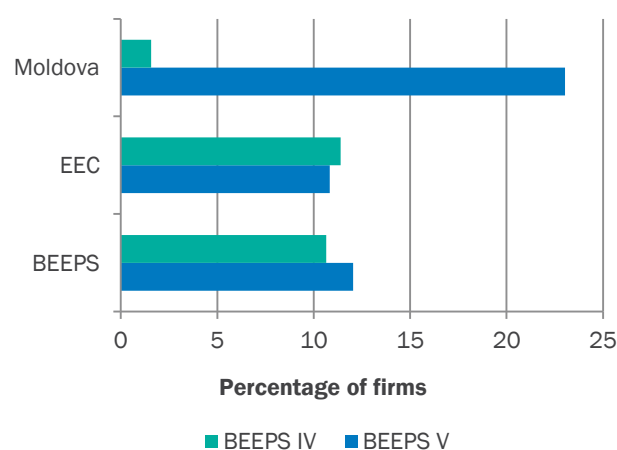
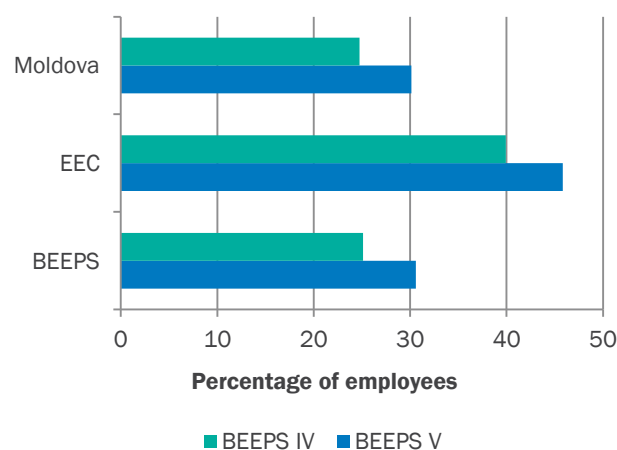


Chart 3. Employees with a university degree



Mongolia

In BEEPS V, the top three business environment obstacles identified by Mongolian firms were access to finance; competitors' practices in the informal sector; and electricity issues (Chart 1). Access to land was among the top obstacles for SMEs, young and manufacturing firms, while large firms were concerned about workforce skills and corruption. In BEEPS IV political instability replaced electricity issues as one of the main constraints.

High collateral requirements and limited access to land in the capital

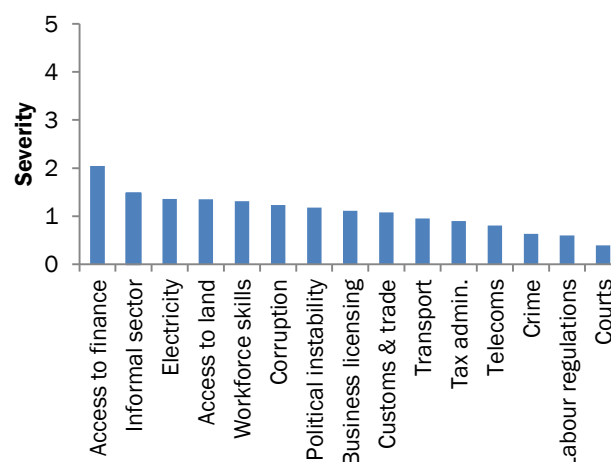
Access to finance remained the top obstacle for Mongolian firms, despite the relatively high share of firms with bank loans (48.1%), well above the Central Asia (CA) and BEEPS V averages. However, out of the firms that needed a loan, 45.1% of SMEs and 61.6% of young firms were credit-constrained – they were either discouraged from applying or rejected when they did. Virtually all recent loans (99.5%) required collateral, the highest share across BEEPS countries. The median collateral value relative to loan value increased fivefold, from only 40% in BEEPS IV to 200% in BEEPS V (Chart 2). High collateral requirements discouraged 9.6% of firms from applying for a loan – all of them were SMEs.

Competitors' practices in the informal sector ranked second place. About 48% of Mongolian firms reported competing against firms in the informal sector, an increase of 5 percentage points compared with BEEPS IV (Chart 3). This puts Mongolia in first place among countries in Central Asia.

Electricity issues were identified as the third most severe obstacle. The wait for an electrical connection, at 94 days, more than quadrupled in BEEPS V compared with 20 days in BEEPS IV. The share of firms reporting that an informal payment was expected or requested to obtain an electrical connection more than doubled to 34.5%. While the share of firms experiencing power outages and the frequency of power outages decreased, their duration increased from 4.3 hours in BEEPS IV to 11.6 hours in BEEPS V, and the associated losses rose from 2.1% to 5.5% of total annual revenue.

Access to land moved from 12th place in BEEPS IV to 4th place in BEEPS V. This is perhaps counter-intuitive given how sparsely Mongolia is populated. However, it is proximity to the capital and land quality that matter. Population density in Ulaanbaatar has been growing in recent years, reaching about 50% of Mongolia's entire population. Approximately 45% of applicants for a construction-related permit reported that an informal payment was expected or requested – almost 14 percentage points higher than in BEEPS IV.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Median collateral required

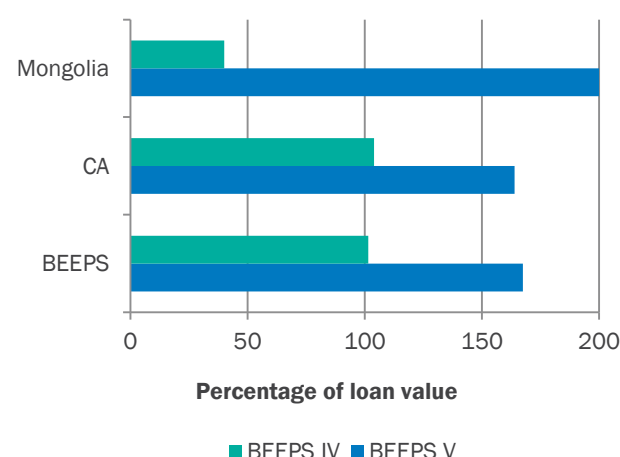
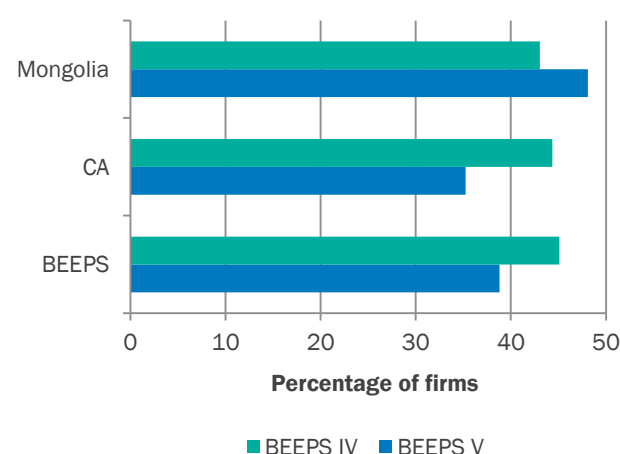


Chart 3. Competition from the informal sector



Montenegro

In BEEPS V, the top three business environment obstacles identified by Montenegrin firms were competitors' practices in the informal sector; access to finance; and electricity issues (Chart 1). Large firms found issues with customs and trade regulations and workforce skills the most problematic. Manufacturing firms found electricity issues to be a more binding constraint than access to finance. In BEEPS IV access to finance was replaced by tax administration as one of the main business environment obstacles.

Fierce informal competition and high interest rates

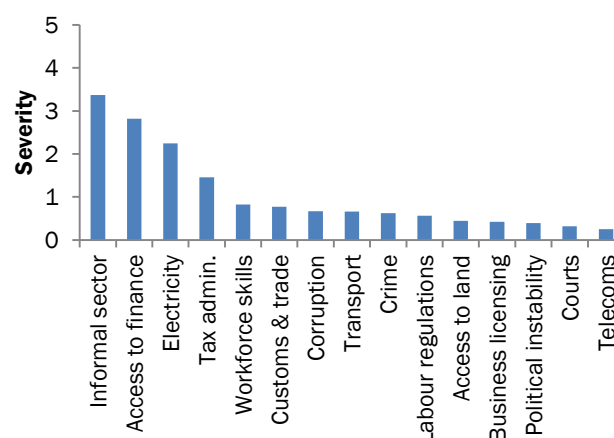
Competitors' practices in the informal sector remained among the largest obstacles to conducting business in Montenegro. The share of firms that reported to compete with firms in the informal sector increased from 27.3% in BEEPS IV to 52.4% in BEEPS V (Chart 2). This may include practices by registered firms, such as paying part of the wages informally and not declaring them to the authorities, contributing to informal employment and affecting the tax revenue of the state.

Access to finance was the second most severe obstacle. Montenegrin firms relied much less on internal funds and retained earnings to finance working capital and fixed assets purchases than their south-eastern Europe (SEE) counterparts (Chart 3). Instead, more than a quarter of working capital and 14% of fixed assets purchases were financed by purchases on credit from suppliers and advances from customers. About 4.9% of the firms relied on non-bank financial institutions (microfinance or credit companies) to finance their fixed assets, more than twice the SEE average of 1.8%. Over half of surveyed firms had a loan, although the median collateral required increased to 240% of loan value, compared with 100% in BEEPS IV. Large firms had relatively good access to finance compared with SMEs: out of more than 90% of them that needed a loan, only 1.4% were credit-constrained, compared with 57.7% of credit-constrained SMEs out of the 57% that needed a loan. The situation was even worse for young firms: out of 56.6% that needed a loan, 96.9% were discouraged from applying for one.

Electricity issues remained among the top obstacles. While the wait for an electrical connection did not change significantly and was below the SEE average, there was a sharp increase in the percentage of firms reporting that an informal payment was expected or requested to obtain it: from 2.7% in BEEPS IV to 19.3% in BEEPS V. In addition, electricity supply became less reliable, with the percentage of firms experiencing power outages rising from 55.3% in BEEPS IV to 74.9% in BEEPS V (almost 20 percentage points above the SEE average), although they occurred less frequently overall and resulted in lower losses than in BEEPS IV.

Survey fieldwork period: February 2013 – June 2013. SEE: Albania, Bosnia and Herzegovina, Bulgaria, FYR Macedonia, Kosovo, Montenegro, Romania and Serbia. Small and medium-sized enterprises (SMEs) have 5-99 employees. Young firms are less than 5 years old.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

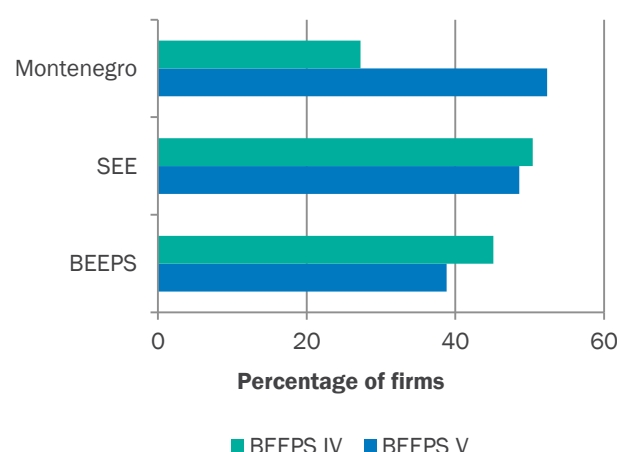
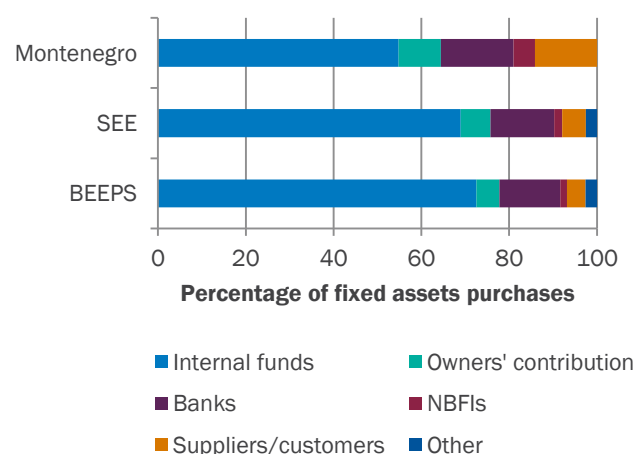


Chart 3. Sources of financing of fixed asset purchases



Poland

In BEEPS V, the three largest obstacles to conducting business, as identified by Polish firms, were tax administration; competitors' practices in the informal sector; and access to finance (Chart 1). Large and old firms cited labour regulations as being a major issue, while young firms considered access to finance, tax administration and courts to be the most binding constraints. In BEEPS IV, political instability, workforce skills and electricity issues were identified as the top business environment obstacles.

Time-consuming bureaucracy

Polish firms viewed **tax administration** as the biggest obstacle. The percentage of senior management's time spent on dealing with government regulations, including taxes, increased from 14.4% in BEEPS IV to 23% in BEEPS V (Chart 2). This is the highest percentage in central Europe and the Baltic states (CEB). The share of firms visited or inspected by tax officials increased from 35.1% in BEEPS IV to 40.5% in BEEPS V. There was also an increase in the share of firms reporting that a gift or informal payment was expected or requested in such meetings, albeit from a low base (1.5%, compared with 0.7% in BEEPS IV).

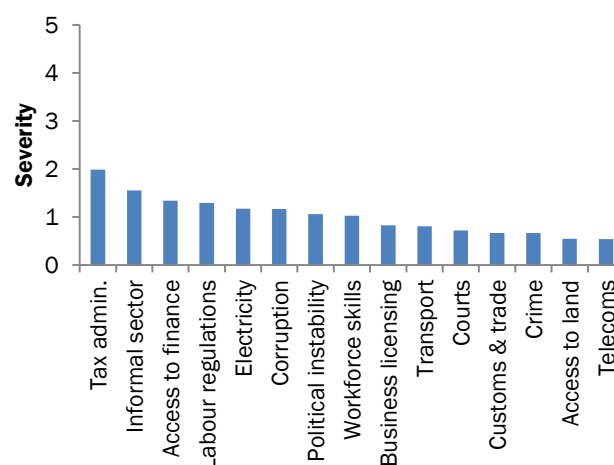
Competitors' practices in the informal sector were also among the three major obstacles. In BEEPS V, 29% of firms reported that they faced competition from unregistered firms, compared with 33% in BEEPS IV.

Polish firms, particularly the young ones, were also concerned about **access to finance**. As elsewhere in the CEB region, the share of bank financing of fixed assets almost halved, to 12.1%. There was also an 18 percentage point reduction in the share of firms with a loan or a credit line, compared with BEEPS IV (from 50% to 32%, Chart 3). The median amount of collateral required as a percentage of loan value increased by 50 percentage points, to 150%. However, the share of credit-constrained firms (those that needed a loan, but either decided not to apply for it or were rejected when applying) decreased from over a third to 26.2%, lower than the CEB average.

Labour regulations were a concern for large and old firms. This could be because of the heavy segmentation of the Polish labour market between permanent and temporary employees. A quarter (25%) of employees are on fixed-term contracts (the highest among the OECD countries, apart from Chile).

Workforce skills no longer featured as one of the top three obstacles to doing business. This is likely to be related to the relatively good performance of the Polish economy during the global economic crisis, when some Poles who had left the country since 2004 returned.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Dealing with government regulations

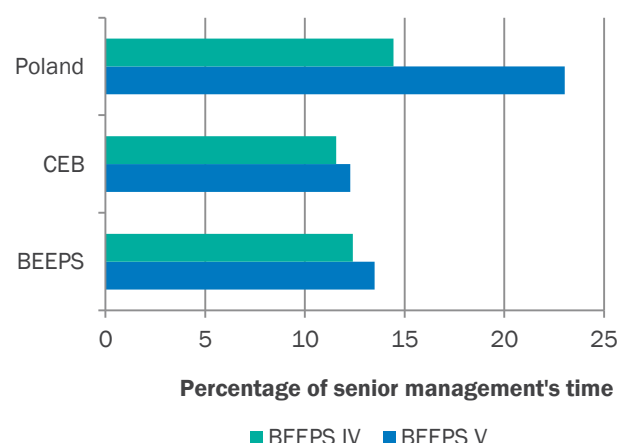
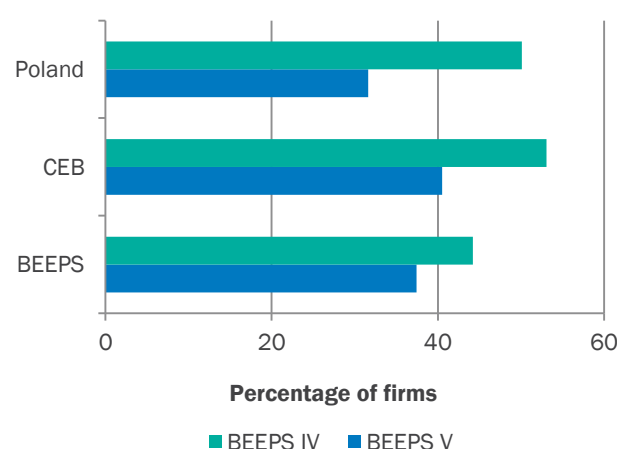


Chart 3. Firms with a loan or a credit line



Romania

In BEEPS V, the top three business environment obstacles identified by Romanian firms were tax administration; corruption; and political instability (Chart 1). Large firms complained about the practices of competitors in the informal sector. In contrast young firms complained more about inadequate access to a skilled workforce. In BEEPS IV, workforce skills were among the top three obstacles however corruption was not.

Despite some improvements, corruption remains a challenge

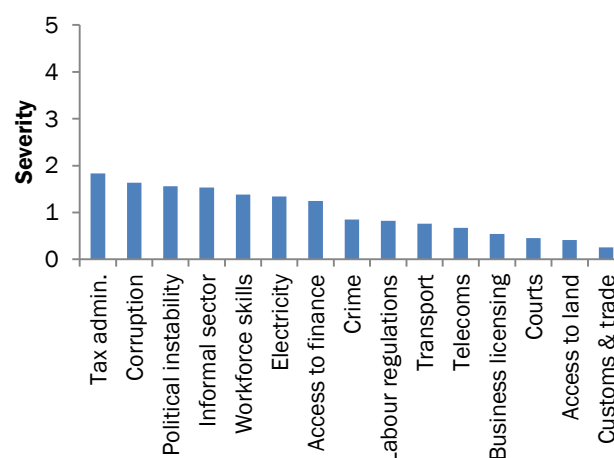
Tax administration emerged as the most severe obstacle. An estimated 18% of senior management's time was spent on dealing with tax regulations, a 6 percentage points increase compared with BEEPS IV, and above the south-eastern Europe (SEE) average of 14.3% (Chart 2). Untaxed, undeclared activity amounts to more than 28% of national output, putting Romania second only to Bulgaria in the EU for the size of the shadow economy as a proportion of GDP. Romania nevertheless made some progress: it reduced the tax payment frequency from quarterly to twice a year and introduced an electronic system for filing and paying taxes.

Corruption remained a serious problem in Romania, despite significant improvements in all corruption related BEEPS indicators since 2008-09. Informal payments or gifts were expected or requested from 13% of firms applying for a construction-related permit, 5.4% of firms meeting with tax officials and 5.8% of the firms applying for an operating licence – all at or below the SEE average, but above the average of fellow EU members in central Europe and the Baltic states (CEB). The firms no longer reported that such payments were expected or requested to obtain an import licence; in BEEPS IV, 16.3% did (Chart 3).

Political stability increased after 2012, when the centre-left Social Democratic Party (PSD) won both municipal and general elections, obtaining a strong majority of seats in the parliament combined with a strong presence in local offices. However, the political environment was adversely affected by difficulties between the prime minister and the then president, which culminated in 2013 in the failed attempt to impeach the latter.

After the country joined the EU in 2007, the number of Romanians migrating abroad increased, especially among young people. In 2010, 3 million Romanians (14.8% of the population) were estimated to be working abroad. In BEEPS V, **workforce skills** were seen as less of a constraint, possibly due to the impact of the economic crisis in Italy and Spain, popular destinations for Romanians working abroad.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Dealing with government regulations

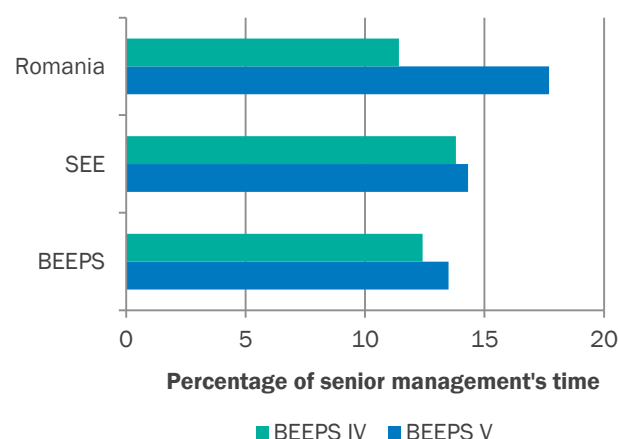
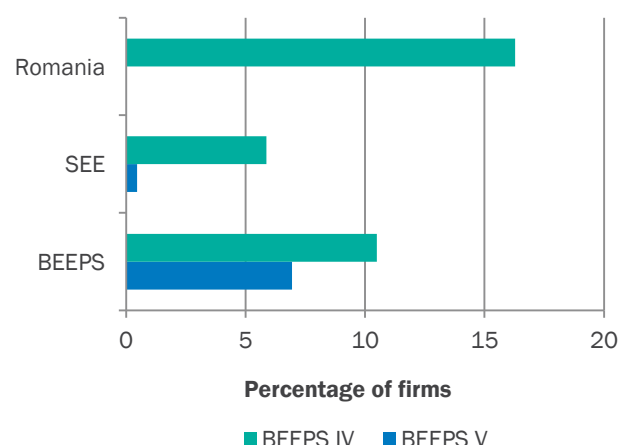


Chart 3. Informal payments to obtain an import licence



Russia

In BEEPS V, the top three business environment obstacles identified by Russian firms were access to finance; corruption; and electricity issues (Chart 1). Competitors' practices in the informal sector were important, too, for SMEs, while large, old and manufacturing firms were concerned about workforce skills. There were significant differences in top obstacles by region.

Limited access to finance for SMEs

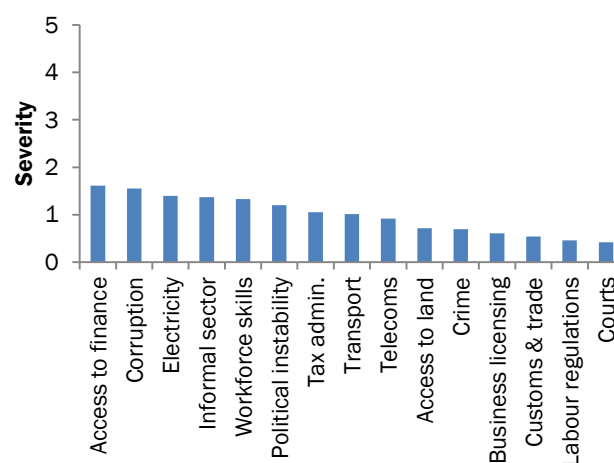
Access to finance was the top obstacle for SMEs and young firms in particular, but was not the most important constraint for large firms. Compared with the other five BEEPS regions, firms in Russia had the lowest share of the firms with a loan or a line of credit. They also experienced the highest rejection rate of loan applications – 26.4% of firms that applied for a loan in BEEPS V were rejected, rising to 30.3% for SMEs. Overall, of 57.6% of firms that needed a loan, 64.6% were credit-constrained (either discouraged from applying for a loan or rejected when they applied) – the second-highest among BEEPS countries. More than two-thirds of SMEs that needed a loan were credit-constrained, compared with less than one-third of large firms.

Though **corruption** moved from the fifth to the second place in terms of relative severity of obstacles in BEEPS V, the results show that the number of Russian firms that reported bribing officials in exchange for specific services decreased in most aspects, with the exception of obtaining an electricity connection. Following the reduction in the number of documents needed for each import transaction and lowering of the associated cost, only 5.2% of firms reported that an informal payment was expected or requested in import licence applications, compared with 48.2% in BEEPS IV. On the other hand, firms reported making informal payments to “get things done” more frequently than in other regions (Chart 2) as well as compared with BEEPS IV.

Electricity issues remained among the top obstacles. The wait for an electricity connection more than doubled, from 58.6 to over 120 days, providing an opportunity for bureaucrats to seek informal payments. The share of firms that experienced power outages and the duration of power outages did not change much in BEEPS V compared with BEEPS IV. Although their frequency decreased from 3.5 to 2.1 in a typical month, the losses resulting from power outages increased from 2.5% to 4.3% of sales (Chart 3).

Workforce skills still appeared among the top three obstacles for large firms. The share of full-time employees with a university degree (57.2%) was substantially higher than the BEEPS average of 30.6%, but the firms may have been complaining about the quality rather than the quantity of workforce skills.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Informal payments to “get things done”

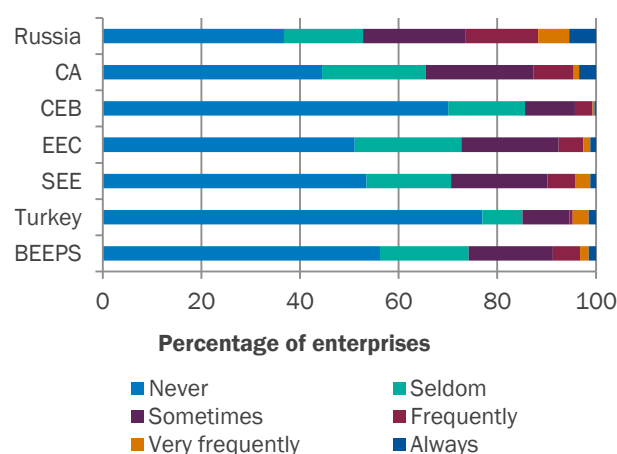
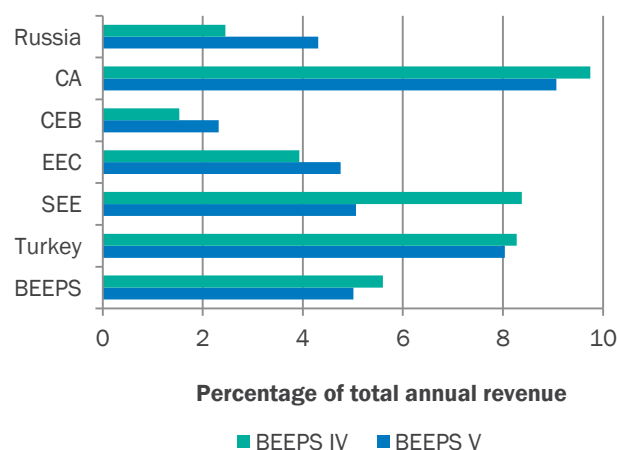


Chart 3. Losses due to power outages



Serbia

In BEEPS V, the top three business environment obstacles identified by Serbian firms were political instability; tax administration; and access to finance (Chart 1). Large firms were concerned about electricity issues and practices of informal sector competitors, while services firms complained about corruption. Tax administration was the top obstacle named by young firms. In BEEPS IV, competitors' practices in the informal sector were among the most binding of business environment obstacles instead of tax administration.

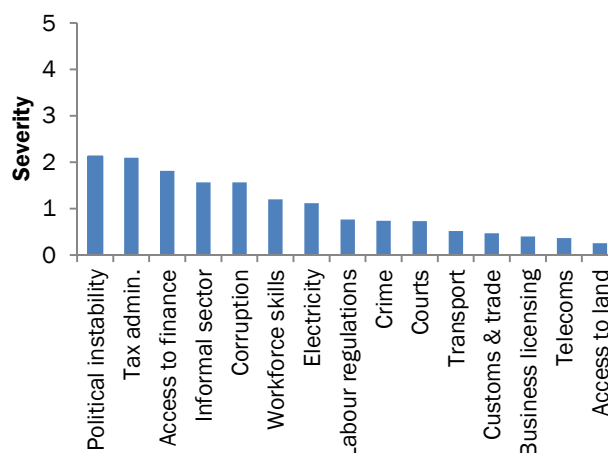
High reliance on euro-denominated loans

Years 2011 and 2012 were characterised by major opposition rallies focused on the economy and widespread corruption, so it is therefore not surprising that **political instability** emerged as the most severe obstacle. Presidential and parliamentary elections, held in May 2012, saw the defeat of the governing Democratic Party and brought to power the largest opposition party: Serbian Progressive Party (SNS), which joined forces in the new government with the centre-left Socialist Party (SPS).

Tax administration moved from the sixth to the second place in terms of severity for Serbian firms. In 2012 the Serbian government passed a fiscal consolidation package, increasing many tax rates and introducing structural reforms in the tax administration. According to *Doing Business*, Serbian firms face a total of 67 payments per year to comply with tax regulations, the most in all of Europe.

Access to finance remained the third most severe obstacle. The share of bank financing of fixed asset purchases decreased from 28.9% in BEEPS IV to 14.6% in BEEPS V; it was compensated by increased reliance on internal funds and credit from suppliers and advances from customers. Unfavourable interest rates were named as the main reason for not applying for a loan in BEEPS V by more than a third of the firms (Chart 2). The share of firms with a loan also decreased, from more than two-thirds to 40%, below the south-eastern Europe (SEE) average of 48.9%. More than half of the outstanding loans were denominated in foreign currency (euros), higher than in all other BEEPS countries, except the Kyrgyz Republic and Tajikistan (Chart 3). The government and the National Bank of Serbia signed the *Memorandum on the Strategy of Dinarisation of the Serbian Financial System* in April 2012, outlining the three groups of measures: monetary and fiscal policy measures geared at strengthening the macroeconomic environment; measures to promote dinar-denominated instruments and markets; and measures to promote the development of foreign exchange hedging instruments.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Reasons for not applying for a loan

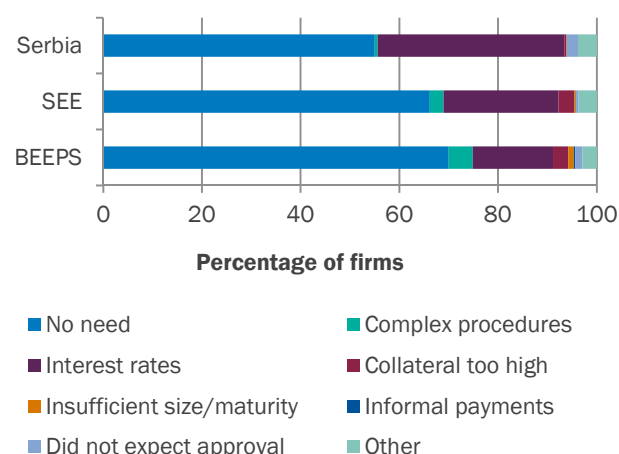
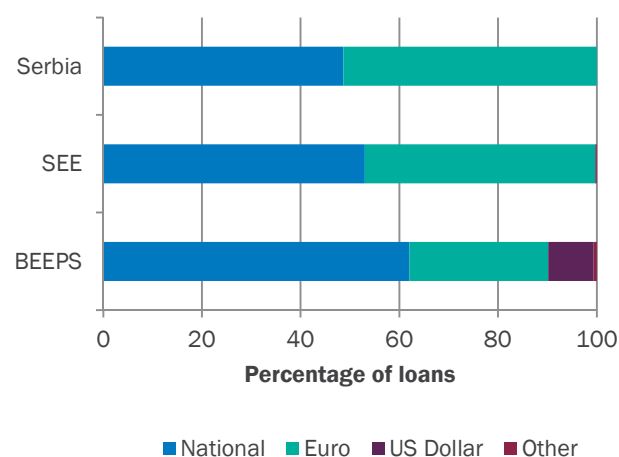


Chart 3. Loans by currency



Slovak Republic

In BEEPS V, the top three business environment obstacles identified by Slovak firms were competitors' practices in the informal sector; electricity issues; and access to finance. SMEs were more concerned about access to finance than electricity issues, while corruption topped the list for large firms, followed by courts and labour regulations. Young firms also complained about crime, theft and disorder. In BEEPS IV crime, theft and disorder were among the top obstacles instead of competitors' practices in the informal sector.

Relatively high energy prices and increased competition with the informal sector

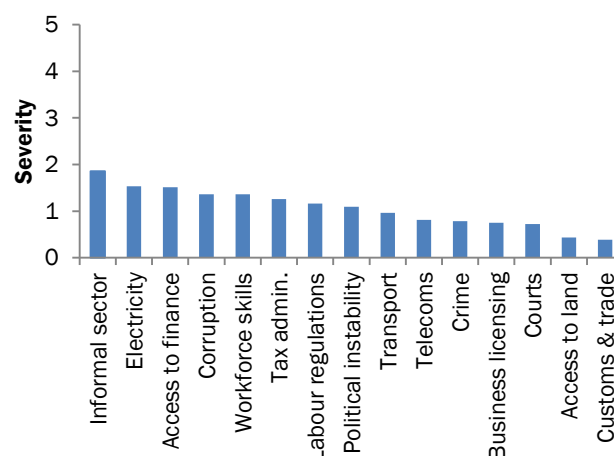
Competitors' practices in the informal sector were identified as the top obstacle facing Slovak firms. The share of firms that reported to compete against informal firms increased slightly, from 40% in BEEPS IV to 43% in BEEPS V, exceeding the central Europe and the Baltic states (CEB) average of 35%.

Electricity issues were the second-most severe obstacle. The wait for an electrical connection, while just below the CEB average, increased from 25 to 39 days. The average number of outages in a typical month was 2.8, higher than the CEB average of 2.3. In addition, the electricity prices are higher than the European Union (EU) average. According to Eurostat, the electricity price for industrial consumers in the Slovak Republic in 2012 was €0.1227 per kilowatt hour (kWh), above the EU average of €0.0942 per kWh.

Access to finance moved from the first to the third place, but remains an important issue, particularly for SMEs. Firms now rely less on internal funding (47% in BEEPS V compared with 59% in BEEPS IV) and more on suppliers/customers in financing fixed-assets purchases; the share of bank financing has not dropped as drastically as in most other CEB countries. The shares of firms with a loan or a credit line as well as the required collateral as a share of loan value remained roughly the same as in BEEPS IV and were above the CEB average.

Workforce skills were also a major concern. The Slovak Republic faces high structural unemployment, particularly among the young and the low-skilled workers. Tertiary educational outcomes as well as vocational training do not match the needs of the labour market. Another explanation for firms complaining about workforce skills could be "brain drain". Emigration to Western Europe increased after the country joined the EU in 2004. The total number of migrants in 2010 was estimated to be more than half a million people (9.6% emigration rate).

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

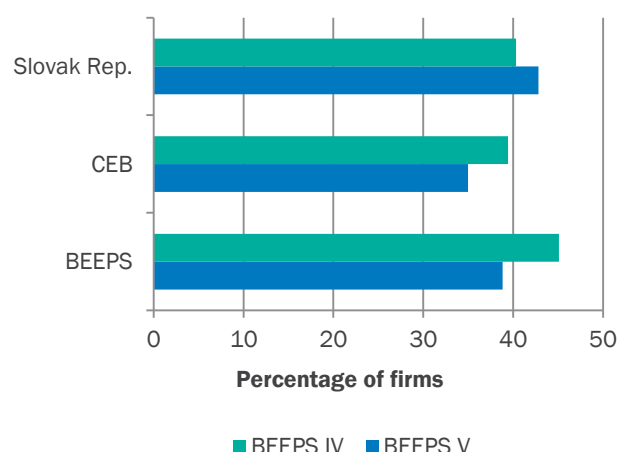
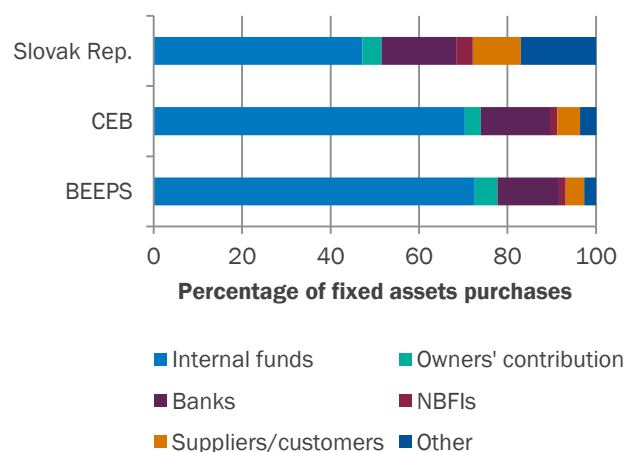


Chart 3. Sources of financing of fixed asset purchases



Slovenia

In BEEPS V, the top three business environment obstacles identified by Slovenian firms were political instability; tax administration; and access to finance (Chart 1). Labour regulations were among the top obstacles for young, large and manufacturing firms. The latter were also concerned about corruption. In BEEPS IV, the top three obstacles were access to finance; competitors' practices in the informal sector; and electricity issues.

Labour regulations continue to be an obstacle, despite some reforms

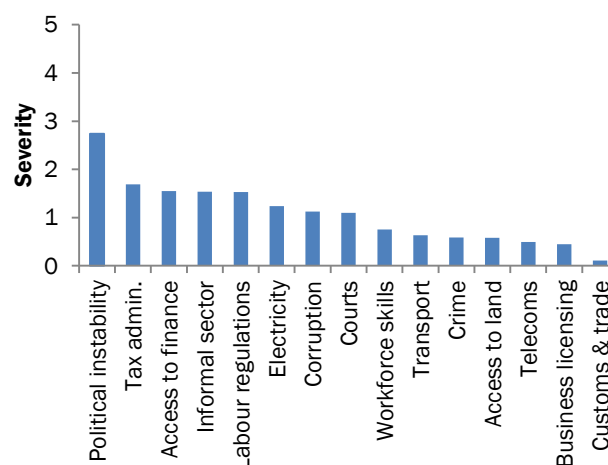
Unsurprisingly, **political instability** was considered to be the most severe obstacle for Slovenian firms. The end of 2012 witnessed massive anti-government protests fuelled by accumulated popular frustrations over a difficult economic situation in the country. At the beginning of 2013 a controversy related to the publication of a report of the anti-corruption commission containing allegations against the head of government led to a political crisis, culminating in a no-confidence vote in the parliament on 27 February 2013.

Tax administration was considered to be the second-most severe obstacle. Although the share of the firms visited or inspected decreased and was relatively low compared with the CEB average, the number of inspections by or meetings with tax officials in those that were examined increased from 1.8 times in BEEPS IV to 2.8 times in BEEPS V, exceeding the central Europe and the Baltic states (CEB) average of 2.2 inspections or meetings (Chart 2).

Access to finance remained among the top three obstacles. Firms financed more than three-quarters of fixed-asset purchases from internal funds or retained earnings. The share of firms with a loan or a line of credit decreased to 65.6%, but was still well above the CEB average of 40.5% (Chart 3). Just over a quarter of the firms applied for a loan and almost 95% of them received it. While the share of credit-constrained firms (those that needed a loan but were either discouraged from applying or rejected when they did) was below the CEB average; it increased by almost 20 percentage points compared with BEEPS IV.

Labour regulations were among the top three obstacles for young, large and manufacturing firms. The labour market in Slovenia is considered to hamper competitiveness and economic adjustment due to the rigidity of permanent labour contracts and complicated administrative procedures. A positive step towards reform was made in March 2013 with the passing of the new employment act which simplifies the process of hiring and firing employees.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Tax official inspections/meetings

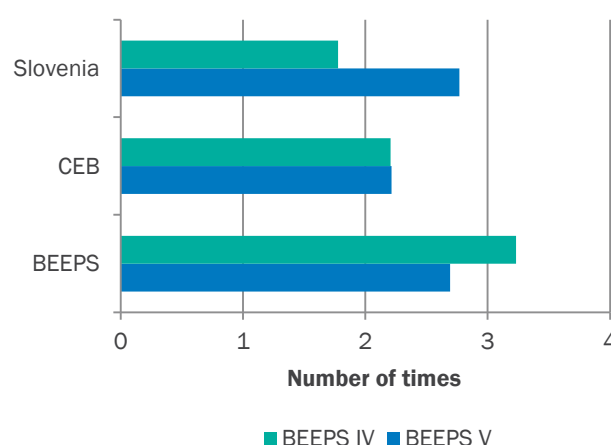
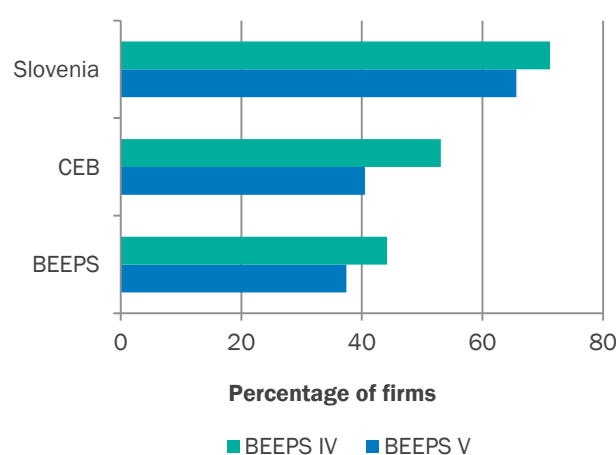


Chart 3. Firms with a loan or a line of credit



Tajikistan

In BEEPS V, the top three business environment obstacles faced by Tajik firms were electricity issues; access to finance; and competitors' practices in the informal sector (Chart 1). Large firms were more concerned about tax administration than access to finance. Young firms complained most about access to finance and political instability. In BEEPS IV workforce skills were in third place. Notably, tax administration was in the ninth place.

Electricity supply and access to finance remain challenging

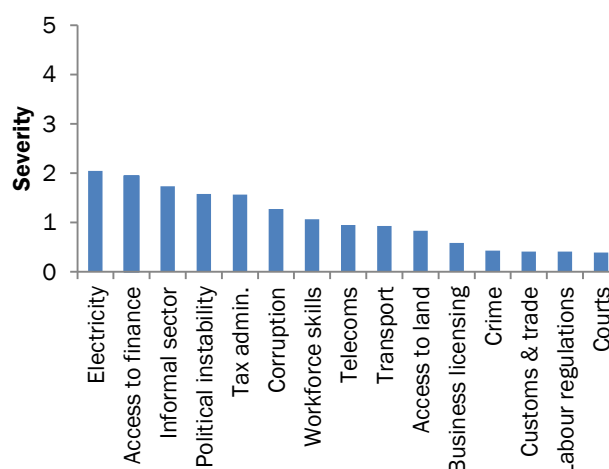
Electricity issues remained the top obstacle for Tajik firms. Although the wait for an electrical connection decreased from 28.3 to 19.2 days, the share of firms experiencing power outages remained close to 60%. The average duration of power outages decreased from almost 10 hours in BEEPS IV to 6.9 hours in BEEPS V, but they were more frequent: firms experienced on average 10.8 power outages in a typical month in 2011, compared with 8.6 in BEEPS IV and 6.5 for Central Asia as a whole. Although the losses of Tajik firms from power outages decreased from 18.8% to 14.4% of total annual revenue, they remained very high compared with the average of 5% of revenue across the covered countries (Chart 2).

Most of the firms in Tajikistan faced limited **access to finance**. Compared with BEEPS IV, they relied more on the internal funds and retained earnings to finance fixed assets purchases. Moreover, a comparatively large share of fixed assets was financed through owners' contributions (14.2%, the highest among the covered countries) and, in turn, a disproportionately small share through bank loans (5.1%, the second lowest after Albania). Overall, only 14.6% of firms had a loan or a credit line in BEEPS V, the lowest share among covered countries along with Azerbaijan. Almost 60% of all outstanding loans were denominated in US dollars, trailing only the Kyrgyz Republic (Chart 3). Real interest rates on loans were on average among the highest and maturities among the shortest in the covered countries.

Competitors' practices in the informal sector remained the third most severe obstacle. The share of firms facing competition from the informal sector remained almost unchanged at around 35%.

It is not surprising that **tax administration** emerged among the top five obstacles in BEEPS V. Compared with BEEPS IV, senior management spent more time dealing with government regulations. The share of firms visited by tax officials and the number of their visits increased and was among the highest in the countries covered. Corruption in tax matters has decreased, but was still much higher than the Central Asia average, trailing only the Kyrgyz Republic and Ukraine.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Losses due to power outages

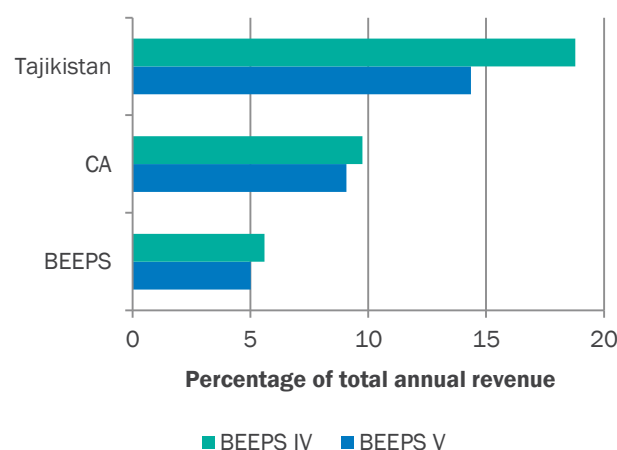
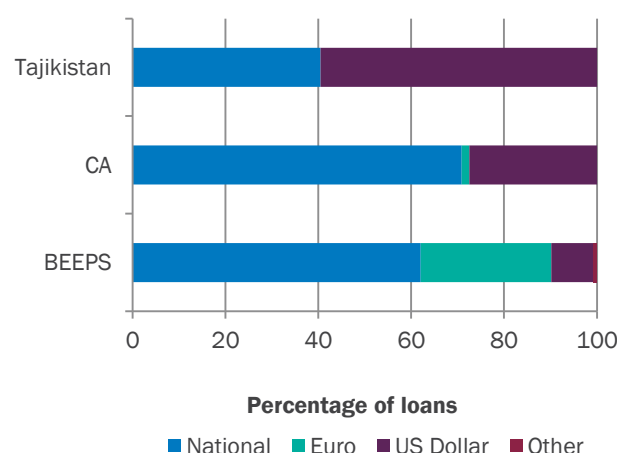


Chart 3. Loans by currency



Turkey

In BEEPS V, the top three business environment obstacles identified by Turkish firms were competitors' practices in the informal sector; political instability; and electricity issues (Chart 1). Large and services firms were most concerned about political instability. Corruption was no longer among the top three constraints, except for young firms.

Concerns about informal sector competitors amid political instability

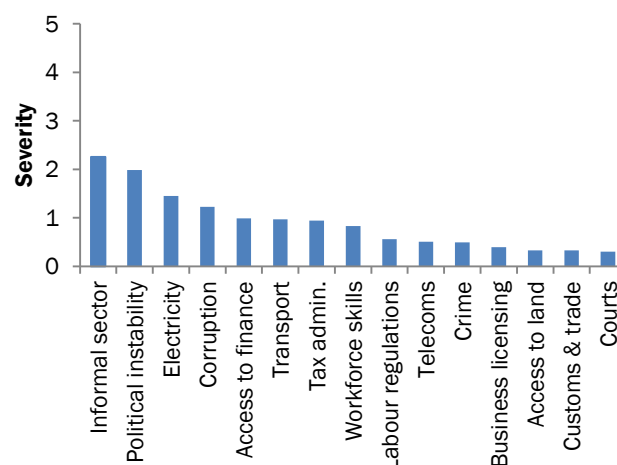
Competitors' practices in the informal sector were the top obstacle faced by Turkish firms. Although the share of firms that compete against unregistered or informal firms decreased from 52.4% in BEEPS IV to 40% in BEEPS V, it still remained slightly above the BEEPS V average of 38.8%. Most affected by the competition from informal firms were large firms (67.5%). 40-50% of the Turkish economy is typically estimated to be informal.

It is not surprising to see **political instability** in second place. The period during which the survey was in the field was characterised by heightened political turbulence, including widespread street protests in the summer of 2013; high-level graft allegations in December 2013; and a formal change of political leadership following the first direct presidential elections in August 2014. These events may have disrupted trade and reduced investments due to uncertainty.

Firms viewed **electricity** issues as the third top obstacle. This is likely due to the 9.8% rise in electricity prices in early October 2012, in line with the by-then rising global energy costs, with the aim to help support public finances. The average number of power outages in a typical month in BEEPS V was 5.4, slightly below the BEEPS IV figure of 5.7, but above the BEEPS V average of 5.2 power outages in a typical month. Moreover, the percentage of total annual revenue lost due to power outages was 8%, exceeding the BEEPS V average of 5% (Chart 3).

The ranking of **corruption** as an obstacle improved slightly, moving from third place in BEEPS IV to fourth place in BEEPS V. There were some improvements on several corruption indicators: the shares of firms that reported informal payments were expected or requested by tax officials declined from 3.5% in BEEPS IV to 0.6% in BEEPS V, below the BEEPS V average of 8.6%. For construction-related permits, this share declined from 7.3% to 0.9%, well below the BEEPS V average of 17.6%. On the other hand, the share of firms agreeing that the court system is fair, impartial and uncorrupted, while above the BEEPS V average, decreased from 65.8% in BEEPS IV to 53% in BEEPS V.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Competition from the informal sector

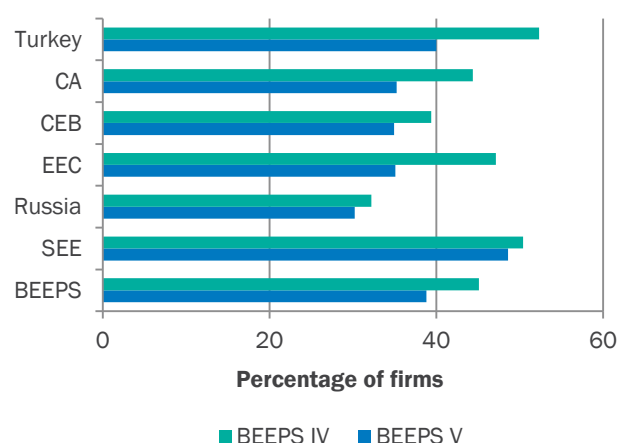
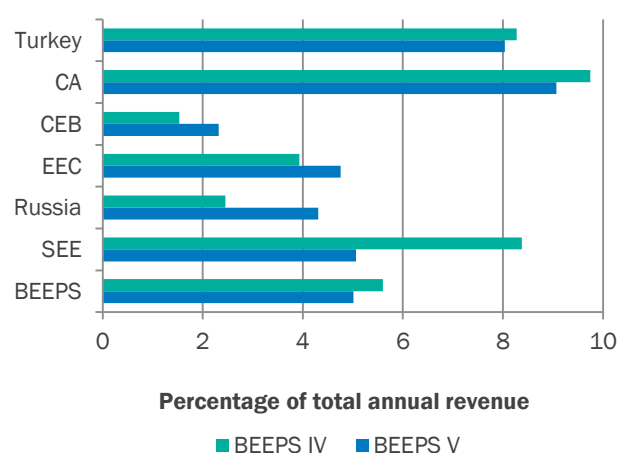


Chart 3. Losses due to power outages



Ukraine

In BEEPS V, the top three business environment obstacles identified by Ukrainian firms were political instability; corruption; and competitors' practices in the informal sector (Chart 1). Large, young and manufacturing firms were more concerned about access to finance than the practices of informal sector competitors. In BEEPS IV, tax administration was in third place.

Political instability and corruption represent challenges

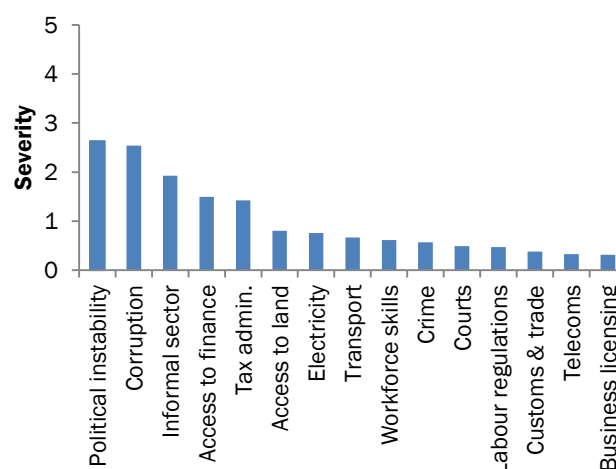
Given the uncertainty about the future of Ukraine's association with the EU, and its evolving relationship with Russia, it is not surprising that **political instability** was perceived as the top obstacle faced by Ukrainian enterprises in BEEPS V.

Closely tied to politics, **corruption** also remained a major issue. The informal payments that firms reported paying to secure government contracts drastically increased from 3.8% to 14.2% of contract value (Chart 2). This put Ukraine in the unflattering first place among the countries covered by BEEPS. The share of firms that reported informal payments were expected or requested grew in all examined cases: when obtaining an electrical connection; construction-related permits; operating licences; in meetings with tax officials, but mostly when obtaining an import licence: this practice grew from 1% in BEEPS IV to over 26% in the latest round. Overall, firms had to pay on average 5.0% of their annual revenue as informal gifts to public officials "to get things done" – by far the largest payment among the covered countries.

Competitors' practices in the informal sector were identified as the third most severe obstacle, with 50% of firms reporting to compete with informal sector firms. This is the second-highest share in the eastern Europe and the Caucasus (EEC) region, after Georgia.

Access to finance remained a problem, too. Fewer than 20% of firms purchased fixed assets in the latest BEEPS round, compared with almost half in BEEPS IV, and they were now less likely to finance such purchases with bank loans. Instead, they relied more on borrowing from non-bank financial institutions, moneylenders, friends, relatives and similar sources. The share of firms that did not apply for a loan because they had no need was the lowest among BEEPS countries at 45.3% (Chart 3). 63.4% of firms reported needing a loan; 72.4% of them were credit-constrained: they either did not apply for a loan (despite needing it) or were rejected by the bank when they did, suggesting that supply-side factors play a relatively large role in explaining the limited borrowing by Ukrainian firms. The situation was even more dire for young firms: out of 52.7% that needed a loan, 92% were credit-constrained.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Informal payments to secure a government contract

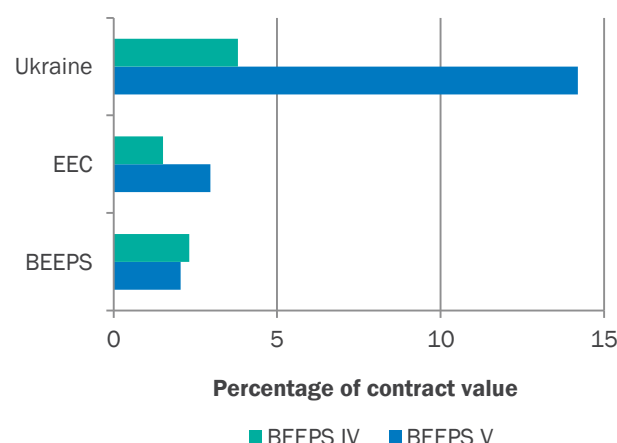
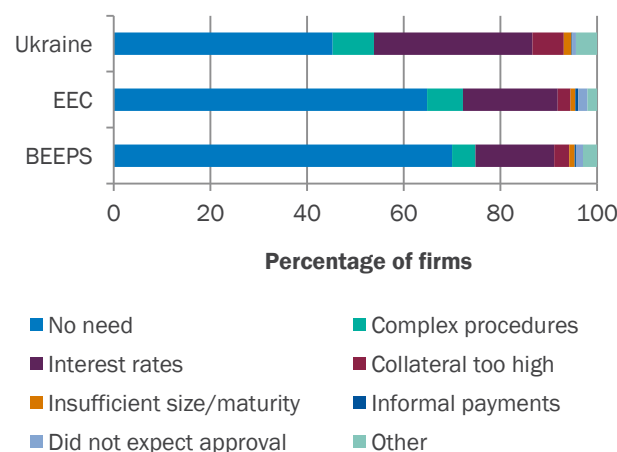


Chart 3. Reasons for not applying for a loan



Uzbekistan

In BEEPS V, the top three business environment obstacles faced by firms in Uzbekistan were electricity issues; competitors' practices in the informal sector; and access to finance (Chart 1). In BEEPS IV crime, theft and disorder; electricity issues; and workforce skills were the most binding constraints.

Worsening electricity supply reliability and poor access to long-term financing

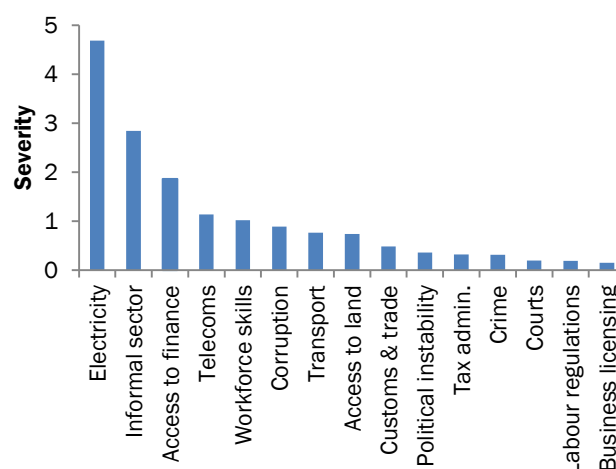
Electricity issues remained a top obstacle to firm performance in Uzbekistan. While the wait for an electricity connection decreased from 28 days in BEEPS IV to six days in BEEPS V and the share of firms that experienced power outages and their duration in BEEPS V decreased compared with BEEPS IV, the average number of power outages more than doubled to 15.3 in a typical month and the share of revenue lost due to power outages increased from 8.9% to 16.0%, the highest among the covered countries. The worsening supply reliability is caused by transmission bottlenecks as well as ageing and increasingly unreliable thermal power plants. According to the World Bank, 40% of the available generation capacity is past or will reach the end of its service life by 2017.

Competitors' practices in the informal sector were in second place, despite the fact that the share of firms that reported to compete against unregistered or informal firms decreased from 39.2% in BEEPS IV to 15.7% in BEEPS V as a result of tight fiscal and monetary policy as well as making it easier to register a business since the previous round. Over the last 10 years the government introduced changes to a tax code and gradually reduced tax levels in some sectors to as low as 5%, while tight import regulations ensure domestic production and consumption leading to greater transparency.

In contrast to BEEPS IV, **access to finance** emerged in third place in BEEPS V. By far the most important source of working capital financing as well as of fixed assets purchases in Uzbekistan were internal funds and retained earnings - 91.9% and 82.3%, respectively. These were among the highest shares in Central Asia. The share of firms with a loan or a line of credit in BEEPS V was higher than in BEEPS IV: 26.4%, compared with 10.5%. However, the average original loan duration was the shortest among the covered countries at 16.8 months.

Crime, theft and disorder moved to the 12th position in BEEPS V. The share of firms that paid for security as well as those that experienced losses as a result of theft, robbery, vandalism or arson on their premises decreased since BEEPS IV, and the losses were half of those they experienced then: 9.3% of total annual revenue in BEEPS V compared with 18.3% in BEEPS IV.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Losses due to power outages

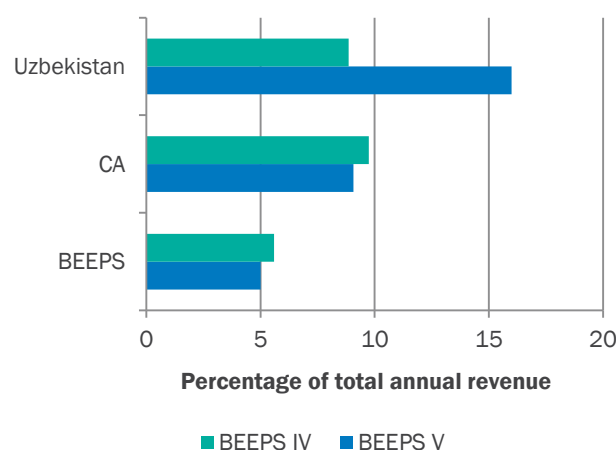


Chart 3. Average original loan duration

