Entrepreneurship in the Western Balkans: Neighbours in Tough Business?

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Abstract:

This study examines the correlates of new self-employment entry and its performance using rich household survey data for Albania, Bosnia and Herzegovina, and Serbia. The results suggest some important similarities and between the three countries. Individuals with some experience in 'the informal sector are more likely to start a formal business in our panels and survive the difficult first year. Moreover, while there is an important role for financing constraints and wealth is positively related to entry, access to formal finance is not significantly related to the entry decision. Moreover, we find that the relationship between entry and remittance receivership is variable, but the evidence does not support it is conducive to self-employment. The evidence favours a competitive view of the informal sector in the Western Balkans, and highlights that further steps are required for external finance by formal institutions to have the desirable impact on private sector development. Even after reforms are introduced, establishing appropriate norms and sets of incentives to nascent entrepreneurs might take a long time.

JEL Classification Codes: J23, M13, O16, O17

Keywords : Self-Employment, Entrepreneurship, Access to Finance, Informality

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1. Introduction

After an extensive period of transition and social change, most households in the Western Balkans rely on the labor market for their livelihoods. However, the performance of the labor markets in recent years has been disappointing. The poor performance is evident even in countries where a number of important labor market reforms have been implemented in the recent past. The participation rates are low, and the unemployment rates are high. Furthermore, the instance of informal sector activity in the "grey markets" is quite common when the regulatory environment provide with better alternative options and adequate monitoring. A number of selected groups bear a disproportionate burden of this environment: in particular, women and the youth bear the largest part of the burden. Given these facts, job creation and a viable entrepreneurial environment are among the primary policy objectives within this region.

A shine of hope in the region is the operation of small and medium-sized firms that dominate the enterprise sector and have contributed to net job creation in several countries (World Bank, 2005a). Until recent years, self-employment was not considered conducive to growth, as it lacked in the emergence of scale economies and the specialization of labor (Blau, 1987). However, this trend has changed, and in the transition countries of Eastern and Central Europe, the small and medium enterprise (SME) sector has been the largest creator of new jobs and the vast majority of these new enterprises are small businesses (McMillan and Woodruff, 2002; Ayyagari, Beck and Demirguc-Kunt, 2004; Klapper, Sarria-Allende and Sulla, 2004). While these new, micro businesses represent a dynamic section of the enterprise sector—with some experiencing very rapid sales growth—there has also been concern about the ability of these firms to survive in the longer-term, secure necessary financing for growth, and thus promote constant and continuous job creation (World Bank, 2007). The dynamics of this group—including the decision to transition into entrepreneurship, the viability of entrepreneurial activity, and the conditions that promote the initiation and survival of such activity—are an important research and policy issue. However, little is known about these dynamics, particularly in the Western Balkans.

Using panel data from the Bosnia and Herzegovina LSMS (2001-2004), a recent work examined the correlates of self-employment transition and viability (Demirgüc-Kunt, Klapper, and Panos, 2009).

Some interesting patterns were revealed, related to the role of access to formal and informal means of finance, remittances from abroad and the experience in 'grey markets'. The study found, among other things, that NGOs and government-supported programs that provide grants and transfers to promote entrepreneurship appear to have played an important role enabling the survival of entrepreneurial activity. This work adheres to this preliminary work, by using LSMS household data to extend the analysis for Bosnia and Herzegovina (*hereafter BiH*) to two neighboring countries, i.e. Albania, and Serbia. The three neighboring countries share several common features in their recent history and transition to market economy.

The results highlight the role of financing constraints. Specifically, wealthier households are more likely to become entrepreneurs and survive the early period of adjustment. However, access to formal means of finance does not have a significant impact on the entry decision in the three countries, a finding highlighting that progress in other fronts is needed for finance to work in the Western Balkans (Johnson, *et al.*, 2000; 2002). After the recent turbulent recent history, the business environment in the three countries is still considered risky. Moreover, some essential conditions for external finance by formal institutions to have the desirable impact on private sector development still need progress. In particular, property rights need to be established and well-defined, in order to provide an essential level of security in a stable macroeconomic environment. Albania, BiH and Serbia still seem to have a long way in that process, as all three rank particularly low in most indicators related to the ease of doing business, contract enforcement and property rights. Even after reforms are introduced, establishing appropriate norms and sets of incentives to nascent entrepreneurs usually takes a long time (La Porta *et al.*, 2000).

Finally, individuals working in the informal sector are more likely to transition to becoming entrepreneurs and more likely to survive in all three countries. The evidence favours a more competitive view of the informal sector in the Western Balkans (Maloney, 1999; Straub, 2005; *inter alia*), as opposed to a segmentation/necessity view, with important policy implications. A potential link between informal experience and later formal entry has important policy implications (Kaufmann & Kaliberda, 1996; Johnson et al., 1997) and can be linked to a number of other arguments, such as: (a) Lazear's (2004) view of entrepreneurs as "jacks of all trades"; (b) the human capital acquisition and skills transferability literature (Guariglia and Kim, 2006; *inter alia*), and (c)

Baumol's (1990) idea of a fixed pool of entrepreneurial talent. In the latter case, the increase in the number of self-employed could conform with the reallocation of that talent in more efficient markets. It is of great further interest to examine if this pattern persists in regression analysis that accounts for household income and other characteristics.

This chapter is organized as follows: *Section 2* of reviews the historic, macroeconomic and institutional background of the three countries, *Section 3* describes the World Bank LSMS data used in the analysis, and the labor force composition in the three countries. Then, *Section 4* presents the empirical strategy for the examination of self-employment entry, along with the list of candidate correlates. *Section 5* presents the summary statistics and estimation results for entry, employment creation and business survival, and *Section 6* concludes.

2. The Labor Market and Business Environment in Albania, BiH, and Serbia

In a snapshot, Albania is a country covering 28,7 sq. km. in area, with a population of 3,6 m. and a labor force of 1,1 m. Bosnia and Herzegovina covers 51,2 sq. km., with a population of 4,6 m. and a labor force of 1,02 m. Finally, Serbia is a country of 77,5 sq. km., with a population of 10,15 m. and a labor force of approximately 3 m. The three neighboring Western Balkan regions in this chapter share the main common feature of going through a difficult path of transition since the 1990s. They have experienced multiple political and economic shocks ever since, along with several reforms at all fronts and importantly their labor markets and business environments.

2.1 Albania

Albania has undergone a major economic reform process in the last decade after a turbulent period, starting from the collapse of the communist regime in 1991 and followed by the financial crisis caused by the collapse of the large pyramid schemes in 1997, and the large influx of Kosovo refugees in 1999. However, the country to a large extend managed to overcome the crises, with strong support from the donor community. By the end of the 1990s Albania had roughly regained its 1990 GDP level, and a satisfactory macroeconomic performance continued after 2000 (World Bank, 2004). Several structural reforms have also been carried out since the late 1990s, and have involved banking, land reforms and privatization. Several small and medium enterprises have been

privatized and significant progress has been made in the privatization of strategic sectors. Despite the persistent efforts, however, poverty in Albania has remained high and per capita income, at around US$1,230 in 2002, has remained one of the lowest among transition economies (World Bank, 2003). Mostly due to the multiple shocks in Albania during the 1990s, per capita income did not exhibit a significant rise even though the economy recorded persistently high growth rates.

Thus, Albania is making the transition to a modern open-market economy lagging behind its Balkan neighbors. Among the negative structural characteristics of the economy are: (a) The country still largely depends on agriculture, which accounts for more than one-fifth of GDP, and is held back because of lack of modern equipment, unclear property rights, and the prevalence of small, inefficient plots of land. (b) The energy shortages and antiquated and inadequate infrastructure contribute to Albania's poor business environment, and make it difficult to attract and sustain foreign investment. (c) The labor market is hampered by a large informal sector. This is due to the large agricultural sector and the impediments in the labor market. Albanians are known to engage in business activities, but most of these seem to take place under the veil of the grey economy. (d) There are huge worker outflows to neighboring countries.

Albania is often characterized as "*a country on the move*", as there are large numbers of legal and illegal immigrants to neighboring countries, mostly Italy and Greece (Carletto et al., 2006; Castaldo et al., 2007). The numbers are indeterminate, as migration is often seasonal or temporary, depending on seasonal employment opportunities and network information. Some estimates suggest that an additional 10% of the 3,6m. population lives and works abroad (CIA World Factbook, 2007), but given seasonal/temporary migration, the authorities in neighboring countries report the numbers are much higher. Other conservative estimates suggest that the number of immigrants from Albania is higher than 500 thousand, and taking into account the waves of seasonal/temporary migration in neighboring countries this number exceeds 1 million workers. The geographical mobility of labor is one of the important adjustment mechanisms that help to cope with poverty, structural unemployment and asymmetric shocks (Zezza et al., 2005). As a result, the economy is also largely dependent on remittances from abroad of $600-$800 million and these figures help offset the towering trade deficit (World Bank, 2006a). The majority of temporary migrants, mainly from rural areas in the Center and the North-East, travel to Greece and Italy to seek short-term employment

opportunities and complement their income from agricultural activities. Furthermore, in recent years the flow of temporary migrants to more distant destinations such as Italy and Germany has increased substantially. According to estimates, an astonishing 35% of households have children or other household members currently living abroad (World Bank, 2004). Almost one-half of Albanian households have access to migration networks, either through direct migration of a household member or through their children living abroad (World Bank, 2003; Azzari et al., 2008).

2.2. *Bosnia and Herzegovina*

Bosnia and Herzegovina (BiH) was established after a tragic 4-year war in the early 1990s that got 6% of a 4.4m population killed or missing, and forced another 60% to relocate. An estimated 1m people have left the country (World Bank, 2005a). The conflict also generated new categories of unemployed and in 1996, the official self-reported unemployment rate was 80%, which decreased to 35% by 2001 (World Bank, 2002). The macroeconomic instability caused by the war was characterized by a 75% drop in per capita GDP between 1990 and 1995, from its initial US$2,400 level to an estimated US$600. In the following years, high nominal rates of economic growth increased the figure to US$1,200 by the end of 2000 and to its prewar levels as of 2005 (World Development Indicators, 2006).

In 1995, the Dayton Peace Accords decentralized BiH, recognizing a second tier of government, comprised of two entities: the Bosniak/Croat Federation of Bosnia and Herzegovina (FBiH) and the Bosnian Serb-led Republika Srpska (RS). Facing massive unemployment and a deficient social welfare system, both entities have since taken major steps to transition to market-economies, with the continuous support of the international community and the donors. Among them, several initiatives were taken to encourage small and medium enterprises by establishing microenterprise credit institutions[1], and important reforms to the regulatory framework for the financial environment and the labor market were introduced in 2000-2001.

[1] The "Microcredit Organization" law passed the FBiH parliament in 2000 and the RS parliament in 2001, establishing a legal and operational framework for microfinance. Furthermore, several microcredit schemes are active and supervised by the international community: notably, the Local Initiatives Project funded by the World Bank, the Micro-Enterprise Bank funded by the EBRD and the IFC, and Quick Impact Program funded by the UNDP/SRRP.

However, the labor market still faces major challenges, such as high and rigid wages in the formal sector, a large and growing share of workers in the informal sector who are not covered by social insurance, and persistent unemployment. BiH has a large informal sector that could account for as much as 50% of the official GDP and half of the registered unemployed. Furthermore, the formal sector remains dominated by the public sector and implementation of privatization has been slow. Further regulatory impediments include high taxation of wages and profits and high employer contributions, difficult access and high cost of credit, and lack of systemic trust in the regulatory and financial environment (World Bank, 2005b). Among the major challenges, labor force participation rates are the lowest in the region, and the incidence of poverty is also among the highest in the area, once again striking primarily the young and the unemployed.

Given these challenging circumstances, the promotion of microenterprise became a political priority, as a gateway out of poverty and/or informality, and as a path to sustainable growth. This priority is also based on the fact that BiH had a large entrepreneurial middle-class in crafts and services before the war, which had a favorable treatment by centrally-planned regime. However, the environment for SMEs is still challenging (World Bank, 2002). In World Bank's Doing Business indicators (2005), BiH's "Ease of Doing Business" ranking is only higher than the ranking of Belarus and the Ukraine among ECE transition countries. In a total of 154 countries, the country ranks particularly low, with respect to ease of starting a business, dealing with licenses, registering property and trading across borders.

2.3 Serbia

Like most former centrally-planned economies, Serbia is also experiencing a difficult transition path to a market-based model. Through a remarkably turbulent recent history of conflict and political change, Serbia is trying to catch up with the more successful reformers in Easter and Central Europe (*ECE*). The three most important challenges the country faces are (a) the lack of employment growth; (b) labor market exclusion; and (c) the ineffective social protection for workers (World Bank, 2006b). The country introduced major reforms in the labor and tax law, aiming to a market-oriented system. The 2001 labor law provided with greater flexibility in hiring and firing, labor deployment, and collective bargaining, changes necessary during transition. The 2001 tax law was a

regressive system that entailed costs for low-wage labor, and raised concerns with respect to the distribution of wealth. Since the restructuring and privatization reforms, job losses have been large and job creation in the private sector has been slow, despite fairly strong economic growth in recent years.

Thus, despite the economic growth observed after 2000, employment remains low, unemployment is high, and the incidence of long-term unemployment is common. Participation rates in the labor market are low and a substantial proportion is working in the informal sector. Similar to its neighbors, the sizeable informal sector accounts for an important share of employment. The low-educated and the young are overrepresented in the 'grey market', the incidence of low-pay and poverty among them is high and the mobility prospects into formal-sector jobs appear low. The result is a weak labor market performance especially when judged by the standards of the more successful transition countries in ECE (e.g., Czech Republic, Slovenia, and Romania). This weakness appears to disproportionately affect young people who have unemployment rates that are among the highest in Europe. Employment outcomes are also considerably worse for women than for men. Very few women work on a part-time basis in Serbia, which is an important type of employment offering flexibility for women in OECD countries. Furthermore, almost one half of the jobs are still outside the private sector. The remainder is largely in the state sector and in socially-owned enterprises. Rural areas are also characterized by high poverty and great mobility in and out of poverty (Ersado, 2006).

Although while in union, Serbia and Montenegro was identified as the top reformer in the world in the Doing Business 2006 report, the investment climate in today's Serbia is still very poor, as international investors rank the country among the riskier to invest (CIA World Factbook 2007). A favorable investment climate is critical for moving through the transition process and stimulating job creation. Despite the reform efforts, Serbia still lags behind in international comparisons in the ease of doing business: its overall ranking is still only 92nd out of the 155 countries included. Finally and importantly, self-employment accounts for one of the lowest shares of employment among CEE and OECD countries.

2.4 *The Business Environment in Albania, Bosnia & Herzegovina, and Serbia Compared*

The World Bank's Entrepreneurship and Doing Business databases provide with some clear indicators of the particular difficulties of the business environment in the three Western Balkan neighbours. Figure 1 presents the rankings of 16 Eastern and Central Europe countries in terms of overall business density and new entry density, from the 2008 World Bank Group Entrepreneurship Survey[2]. The figures are averages for the years 2002-2004 (for consistency with the LSMS databases used in the next section). New business entry density is shown on the vertical axis shows and overall business density is shown on the horizontal. Both figures are numbers per 1,000 of working age population.

Albania, BiH, and Serbia obtain the three lowest ranking when it comes to total business density, among the sixteen countries presented. Albania has figures of 5.439 businesses per 1,000 and 0.421 new businesses per 1,000 working age individuals. The respective figures in BiH are 6.772 total businesses per 1,000 and 0.486 new businesses per 1,000 working age individuals. Serbia does only slightly better when it comes to new entry, with 9.652 total businesses per 1,000 and 0.874 new businesses per 1,000 working age individuals. Its ranking is the third lowest for total business density, after Albania and BiH, and the sixth lowest when it comes to new entry density. BiH and Albania also obtain the lowest ranking in the new entry density figures. Thus, the three counties have the lowest ranking in terms of total business density in ECE, and also rank particularly low with respect to new entry density. Albania and Bosnia and Herzegovina have the two lowest rankings for the years 2002-2004 and Serbia the 6th lowest ranking in terms of new entry density,

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[2] The 2008 World Bank Group Entrepreneurship Survey measures entrepreneurial activity in over 100 developing and industrial countries over the period 2000-2007. It is a joint effort by the World Bank Development Research Group, the IFC, and the Kauffman Foundation in its third year. The database includes cross-country, time-series data on the number of total and newly registered businesses, collected directly from registrar of companies. For more details, see Klapper, *et al.* (2007), and http://rru.worldbank.org/businessplanet/default.aspx?pid=8.

The 16 countries presented in Figure 1 are: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Georgia, Hungary, Latvia, Lithuania, Moldova, Poland, Romania, Russian Federation, Serbia, Slovak Republic, Slovenia, and Ukraine. 2002-2004 averages are presented for reasons of comparability with the LSMS data that will be introduced in the next section.

ranking higher than Georgia, and only marginally higher than Ukraine and Poland. The rankings are indicative of a regional effect that has not changed in later years in the data.

[Insert Figure 1 about here]

This low performance can be complemented by a somehow predictable picture in the World Bank's Doing Business indicators[3]. The ranking for the three neighbours in the year 2009 is shown in Figure 2. In a total of 183 countries, all three countries rank below the median, with respect to ease of doing business, dealing with licenses, employing workers, paying taxes, and enforcing contracts. Bosnia and Herzegovina appears to have a lower ranking in most fronts. However, the three countries perform remarkably better with respect to the ease of getting credit and somehow better when it comes to protecting investors. These features are both really important to the health of the business environment. However, similar pictures can be obtained for the rankings in previous years.

[Insert Figure 2 about here]

Given the poor performance of the three neighboring countries in the business environment indicators, it is of great further interest to examine the correlates of new business entry at a microeconomic level. The next sections utilize the World Bank Living Standards Measurement Surveys in an effort to shed some more light on the origins and characteristics of new self-employment entries in the three countries.

3. The Data: World Bank Living Standards Measurement Surveys

This remaining of this chapter employs household panel data for Albania, Bosnia and Herzegovina, and Serbia. The three data sources are all part of the the World Bank Living Standards Measurement

[3] The World Bank's *Doing Business* project looks at small and medium-size companies and measures the regulations applying to them through their life cycle. The 2008 report covers 10 indicators sets in 181 economies with the goal to provide an objective basis for understanding and improving the regulatory environment for business. *Doing Business* provides a quantitative measure of regulations for starting a business, dealing with construction permits, employing workers, registering property, getting credit, protecting investors, paying taxes, trading across borders, enforcing contracts and closing a business, as they apply to domestic small and medium-size enterprises.

Survey (LSMS) Programme, a multi-year collaborative project amongst the World Bank, other international institutions and several national statistical agencies, aiming to strengthen the government capacity to collect, analyze and disseminate statistical data for poverty monitoring and policy evaluation[4]. The sample period examined is similar for the three countries, and the coverage in terms of the years is subject to data availability. Thus, the period 2002-2004 is covered for Albania, 2001-2004 for Bosnia and Herzegovina, and 2002-2003 for Serbia. The data for BiH is also representative at the entity level. The data for Serbia does not include Montenegro which was still part of the union at the time, and also excludes Kosovo. The samples are representative at the country level, and for urban, rural and mixed municipalities. This unique collection of household panel surveys provides rich demographic and socioeconomic information, and importantly an insight into labor market dynamics in the three countries.

We employ the labor force population, aged 16-65 at the time of the interview, and classify them into mutually exclusive groups according to their employment status every year. We further select the balanced panels for the three countries, in order to obtain an insight on the dynamics in the labor market by individuals who were continuously present in the surveys. This exercise provides with 3,550 individuals observed over 3 years in Albania (10,650 observations); 4,772 individuals observed for 4 years in BiH (19,088 observations), and 3,708 individuals in Serbia, observed for 2 years (7,146 observations).

Following the design of the questionnaire, we define self-employed individuals as individuals describing their status as owner/co-owner of: (i) an enterprise/small business which employs workers ("employer"), (ii) an enterprise/small business which does not employ workers ("own account"). (iii) We identify "formal" self-employment, as individuals who fall into the categories above and also declare work-related characteristics such as earnings and hours in self-employment and whose tax, pension and/or health contributions are paid. In case these criteria are not satisfied, then the individual is classified as informally self-employed.

Standard ILO definitions classify a person as employed if they are presently working or on leave from a job. According to the ILO classification, the informal economy consists of units engaged in

[4] For more information on the LSMS data and for the design, the methodology and the samples in the 3 countries under examination, see Grosh and Glewwe (1998) and the documents in: http://www.worldbank.org/LSMS/.

the production of goods or services to generate income and employment for themselves. These units typically operate at a low level of organization, with little or no division between labor and capital as factors of production and on a small scale. Labor relations – where they exist - are based mostly on casual employment, kinship or personal and social relations rather than contractual arrangements with formal guarantees. According to the ILO, the informal sector can be regarded as a group of operational units that form part of the household sector as household enterprises or unincorporated enterprises owned by households. In addition, the economic literature commonly uses other operational definitions of the informal sector. One of the widely used definitions is based on the status of a household enterprise, which being informal, is often not registered with local authorities, and as such remains outside the official institutional framework.

For the purposes of this chapter, we distinguish between the formal and the informal sector workers among the group of employed. We define employees in formal sector paid employment as individuals working in public enterprises and international organizations, as well as those in the private sector whose pension and health insurance contributions were paid. Informal sector employment comprises of three groups: (a) unpaid supporting family members, and workers engaged in other activities, such as the sale of agricultural products; (b) workers not employed by public enterprises (or state sector) for which pension and/or health contributions are not paid; (c) workers declaring any other out-of-employment activity, but reporting earnings or hours of work. This definition meets previous official classification criteria and informal sector estimates (World Bank, 2002; *inter alia*). By default, the unemployed are those who do not have a job at present, are actively searching for employment, and are able to take a job if it were offered to them. Finally, farmers in own farm and workers in agriculture are classified as a distinct group. All others of working age are classified as inactive.

The classification exercise described above for the 3 balanced LSMS panels in Albania, Bosnia & Herzegovina, and Serbia renders the composition of the labor force for the population with replies in all waves of the surveys. Unemployment – inactivity comprises of a quarter of the working age population with replies in all waves of the LSMS data in Albania and Serbia, while the figure is close to 40% in Bosnia and Herzegovina. The former two countries also have a larger agricultural sector.

The figure is 33.2% in Albania and 17.3% in Serbia. The figure for individuals declaring occupations in agricultural activities is much smaller for Bosnia and Herzegovina (5.6%).

While agriculture dominates the labor market in Albania, formal employment is the second largest activity, with a third of the employed population (17% of the workforce in the balanced panel) working as employees in the public and private sector. One-fifth of the employed population (13% of the workforce) engages in informal employment activity, with one-third of that (4.9%) conducting informal self-employment activity and two-thirds (8.1%) being informal employees or supporting a household business. Formal self-employment comprises of 6.8% of the working-age population.

The literature has claimed that Albania is a country where the residents are keen on being involved in business activities, but fails to distinguish between the formal and the informal sector. Taking into account the additional 4.9% that engages in informal self-employment and the vast amount of people that operate agricultural-household businesses, the figure for people operating in business-type activities is indeed high. Moreover, 10.5% of individuals in the sample declare their status as unemployed and 14.3% declare their status as be inactive. These figures are close to the official statistics. Finally, an additional 5.2% of the population classify themselves as employed abroad. Adding that figure to the numbers of individuals in the informal sector, the total figure for individuals with undetermined informal activity comes close to 20% of the population, a size that is similar to the informal sector in Bosnia and Herzegovina.

[Insert Figure 3 about here]

However, the situation differs somewhat in Bosnia & Herzegovina, mostly due to the structural characteristics of the country. The post-war syndromes are quite evident in the country, as a large number of people were forced to relocate within the region. Furthermore, the instance of disability and the amount of people dependent on social assistance increased substantially. Thus, both figures for unemployment and inactivity are massive, close to 20% each, with a total of 41.2% of the sample being out of employment. This is a very high figure, certainly among the highest in Europe and is well behind the E.U. Lisbon employment standards of 70% to be achieved by the year 2010. The unemployment rate is more than double the EU-15 average and higher than the EU-10 average. Agricultural activity appears quite limited (5.6%), a fact that is also due to geographical reasons.

Given these two facts, informality appears to be a prominent gateway out of poverty. The figure is close to a third of the employed population (17.8% of the workforce). This figure contains both informally self-employed and employees, as in contrast to the other two countries, the data for BiH does not allow a distinction between the two types of activity. One-half of the employed population (31.3% of the workforce) engages in formal paid employment activity. Finally, the figure for formal self-employment is quite small (4.1% in total, in the balanced panel). An interesting feature is that half of the formally self-employed classify themselves as employers. This can be attributed to either the incentives provided by funding projects for the creation of employment, or the history of the region. Before the war, BiH had a large entrepreneurial middle-class. Compared to most centrally planned economies in Eastern Europe, the regime in the former Yugoslavia had a somewhat different treatment of small businesses, mostly those related to crafts and services. These were encouraged and provided with financing mostly from local government-owned banks. Their interests were further supported through the formation of local and politically influential crafts unions. Furthermore, BiH was a location where the former regime placed heavy manufacturing industries, on which socialist regimes placed a huge emphasis.

A similar situation with respect to self-employment arises in Serbia, where nearly 5% of the balanced sample declares their status as self-employed paying taxes and contributions. Less than a third of these are employing others in their business, while 71% (3.3% of the sample) are own-account self-employed. An additional 4.3% appear to be informally self-employed. Previous self-employment estimates give a figure of 7.5% self-employed in Serbia (World Bank, 2006b), however without distinguishing between formality and informality. The figure is clearly quite low, given the self-employment rates of about 14% in the OECD and EU-15, and over 10% in other Eastern-European economies, like Slovenia, Hungary, Poland, and the Czech Republic. The figure for the size of the informal sector in Serbia is close to 12% using the definition adopted for this report, i.e. a bit less than one-fifth of the employed population. The largest fraction of individuals declares their status in formal paid employment, i.e. 41.8% of the individuals in the balanced sample. While the figure is encouraging, one of the well-known problems in Serbia is that the public sector is still among the largest employers, and the process of privatization has not proceeded adequately. Finally, and additional 17.3% of the sample are performing agricultural activities.

The labor force classification used in this report allows us to directly observe transitions to self-employment from year to year. We are able to identify 156 new entries in the three years of the panel for Albania, 222 entries into self-employment status during the course of the four years in the BiH panel, and 88 new entries in the two years of the Serbian panel (Table 1). The figures for the sub-samples of household heads in the three countries are 74, 110, and 38, respectively[5]. Of further interest are the outcomes of the new entries, as business start-ups bear the higher risk of failure during their first years of operation. Indeed, nearly 40% (40 out of 98 new entries of the year 2003) of the newly self-employed in Albania and close to 50% in BiH (87 out of 178 new entries in the years 2002-2003) do not make it through their first year in business. This is a pattern observed in both samples of individuals and household heads.

[Insert Table 1 about here]

These high failure rates could indicate that self-employment entry in BiH is likely to be the outcome of necessity, rather than that of opportunity and motivation. While this interpretation can not be rejected a priori, it is questionable why an individual would undergo the pains of starting a formal business for a short period, in countries where this is not a particularly easy process, and informal operation of businesses is very common. Moreover, our data suggests that there are large welfare gains for individuals operating in formal self-employment that do not indicate necessity. Table 2 presents some welfare indicators by labour market status, for individuals in the sample. The statistics are averages for the years in each sample. It is evident that self-employed individuals rank higher with respect to most welfare indicators. This is the case for both the self-employed that create employment for others, and the own-account self-employed, with the former group clearly ranking the highest in all indicators. The self-employed enjoy higher wages and household income/consumption. Moreover, they rank highly in the income, housing and life satisfaction responses. What is evident from this simple inspection of the data is that the unemployed and the individuals in the informal sector are the two poorest groups that are also the least satisfied with more aspects of life. Thus, the transition to self-employment is related to higher standards of living and formal entry does not appear to be of the necessity type, at least in terms of welfare.

[5] This latter sub-sample is of interest, despite reducing the number of observations, because it is likely to capture new business openings and exclude participation in family enterprises. All results presented in this section are robust to the examination of the household head sample and are available upon request.

[Insert Table 2 about here]

In the next sections of this chapter, we examine the correlates of new self-employment entry in the three countries in more detail. The emphasis is placed on the role of labor market experience and issues of access to finance and financing constraints.

4. Background and Empirical Strategy

The importance of legitimate business operation for employment creation and growth has been emphasized in the recent literature, particularly for economies in transition. Conceptually, the self-employed can be considered as the smallest, but initially most vital unit of entrepreneurial activity. Furthermore, in the previous section it was shown that the self-employed are less likely to experience poverty and relative deprivation. It was further shown that all three countries experience low rates of formal self-employment, compared to other ECA and OECD countries. It is thus of interest to examine the characteristics of the individuals that decide to make the transition to formal self-employment in this challenging environment. Moreover, the interaction of this decision with financial constraints, access to finance, and labor market experience will be explored.

In the first stage of our analysis, we compare differences in human, social and financial capital between groups of new entrepreneurs and individuals who did not become self-employed. Entrepreneurship has been linked to both economic and social attributes. The literature has distinguished between the role of institutions, socioeconomic factors, individual characteristics, and psychological factors, in identifying the correlates of the decision to start an entrepreneurial activity (Djankov et al., 2005, 2006a, 2006b). Other studies emphasize the importance of labor market characteristics (Earle and Sakova, 2000; Dutz et al., 2001), as well as financial wealth and constraints (Paulson and Townsend, 2004; 2005; Paulson et al., 2006). Moreover, we examine the differences between those new entrants that also create employment for others and those that operate as own-account self-employed. Finally, we investigate the correlates of survival in self-employment for more than one year, comparing individuals who made it through their first year as small business operators and individuals who exited before their second year in business.

Our empirical strategy in the regressions examines the relationship between new entry into self-employment in later years of each panel, by individuals not self-employed in the first year, and a set of characteristics of interest. The dependent variable (*Newly Self Employed*) takes the value 1 if the individual started his/her own business, and 0 if not. Our preferred model to examine the relationship between entry and individual and household characteristics is the probit model. The explanatory variables include a vector of the socioeconomic characteristics, such as gender, urban or rural region of residence, a second order polynomial in age, marital status and the logarithm of the number of children, education, and health. Moreover, we distinguish between entities in BiH (*Federation of BiH* vs Republica Srpska). Finally, in order to control for within family effects in self-employment transitions we examine the impact of the presence of another self-employed member in the family.

In separate specifications, we examine the impact of household financial wealth, the relationship with financial institutions, as well as the role of labour market experience and origins. The wealth proxy we use is the logarithm of equivalized per capita household consumption, which is calculated by adjusting household consumption to the number of equivalent adults and deflated using the regional poverty line[6]. In transition countries, income under-reporting and non-reporting biases the calculations based on income. We therefore utilize household consumption in the beginning of the

[6] Income is often considered to be the preferred measure. But income suffers from several defects both in theory and in practice. First, income can be highly volatile, whereas consumption is more readily smoothed by individuals, and thus shows more closely the welfare level of an individual at any given time. Second, in transition economies, such as BiH, people are often paid irregularly and wage arrears are common. In this context, consumption is smoothed while income is erratic.

Our main welfare aggregate is total per capita consumption in current 2001 prices. It includes the following expenditure groups: food, alcohol & tobacco, clothing, housing/utilities, furnishings/household equipment, transport, communications, recreation, education, hotels/restaurants, and other miscellaneous expenses. It excludes health expenditure, to avoid the presence of outliers. The equivalized measure is calculated by adjusting household consumption to the number of equivalent adults: $EA=(A+aK)^{\theta}$, where A: number of adults; K: number of children; a: economies of scale parameter; θ: share of public goods consumed parameter. Finally, the measure is deflated at the regional level using the regional poverty line. For full information concerning welfare in Bosnia and Herzegovina and the construction of the 2001 consumption aggregates, see "Welfare in Bosnia and Herzegovina, 2001: Measurement and Findings", available at: http://siteresources.worldbank.org/INTLSMS/Resources/3358986-1181743055198/3877319-1190298527311/BiH_ANNX_poverty10a_updated.pdf

panel as an indicator of overall financial wealth. The use of other wealth proxies, such as property ownership or the ability to "make ends meet", does not change our main results.

In order to examine the labor origins of the new business entries, we create a set of variables capturing labor market status in the first year of each panel. *Formal Sector Employment* takes the value 1 if the individual was employed in the formal sector, and 0 if not. *Informal Sector* captures individuals operating in the informal sector, and *Unemployed/Inactive* the individuals who were either unemployed or inactive. *Agriculture* and *Employed Abroad* (for Albania only) are the last two categories of labor market origins. These variables and their interactions with other individual and household characteristics are likely to shed some light in the "push" and "pull" aspects of new business entry in the three countries. Moreover, as the incidence of wage arrears is common in transition economies in ECE, we also distinguish between employees in the formal sector who received delayed payments or lower pay than usual, and those who did not. In many transition economies people are often paid very irregularly, with several months of wage arrears being common (Earle and Sabrianova, 2002; Kim, 2005; Boyarchuk et al., 2005; *inter alia*) and average accrued and paid wages diverging significantly. Our data suggests that 9.2% of the population in Albania, 12.3% in BiH, and 8.9% in Serbia receives delayed or unusual payments. These figures correspond to almost half the individuals in formal paid employment in Albania, a third in BiH, and less than a quarter in Serbia (see *Table 3*). Indeed, problematic payment might alter the set of incentives for paid employees in the formal sector, and their transition to self-employment might be motivated more by necessity rather than by any other reason.

Our last set of characteristics of interest is related to access to finance, either formal or informal. Departing from Paulson and Townsend (2004) and Demirgüc-Kunt et al., (2009), we utilize household affiliation with particular financial institutions and sources of finance in the past and examine their impact on the likelihood of starting a new business. We include a dummy *Micro Loan* equal to 1 if the household received a loan from a microcredit institution (such as a credit union, cooperative, or NGO) in the first year of each panel. We also identify households that received a loan from a bank or government agency, *Bank Loan*, and households that received a loan from a family member, friend or other individual early in each panel, *Informal Loan*. The figures for bank loans are 0.9% in Albania, 11.8% in BiH, and 5.6% in Serbia. 0.3% of the population received a loan

from a microcredit institution, and 2.6% in BiH. Finally, the figures for informal loans are 13% in Albania, 17.2% in BiH, and 4.5% in Serbia.

We further examine the relationship between remittances and the switch to self-employment with two variables which importantly distinguish between international and domestic remittances: *Domestic Remittances*, which equals 1 if the individual belongs to a household that received any money, gifts, or services from friends or family working in the same country; and *Remittances from Abroad*, which equals 1 if the household receives money, gifts or services from friends or family working. While most of the literature considers remittances from abroad as the variable of primary interest, we are also interested in remittances from within each country. This is because following in the turbulent recent years in the Balkans, both the numbers of individuals who immigrated abroad and those who were either displaced or chose to migrate within the country were very large. Albania and Bosnia & Herzegovina in particular, are characterized by very large waves of international migration that is a major source of remittances from abroad entering those countries. The impact of remittances from abroad on economic activity and consumption is large (Castaldo and Reilly, 2007), but when it comes to the labor market and the motivation to participate and be productive, the effect of remittance receivership does not go without debate.

Our estimates indicate that 11.8% of the individuals in the sample for Albania, 8.2% in BiH, and 6.9% in Serbia receive some form of remittance domestically. The figures for remittances from abroad are: a striking 32.4% in Albania, 11.9% in BiH, and 6.5% in Serbia. Another striking figure for Albania concerns the volume of remittances received among receivers. Those receiving money from friends and family abroad declare that they receive an amount of money that amounts close to 40% of consumption per equivalent adult in BiH and Serbia. However, the volume of remittances received in Albania amounts to 32 times the consumption per capita. Thus, the volume received is much higher in Albania, and the figure is plausible, given the differences in the salaries between Albania and its neighboring E.U. countries that receive the highest fractions of immigrants from Albania. Thus, in separate specifications, we incorporate variables for the amount of remittances received as a fraction of household consumption, in order to allow for potential non-linearity in the relationship between remittance receivership and business entry.

We finally identify individuals that receive money from humanitarian and religious institutions that do not need repayment (*Institutional Remittances*). These are of specific interest, because they include grants from foreign NGOs and citizen associations provided specifically to promote self-employment and entrepreneurship (Lyman, 2005). Finally, we include a dummy variable, equal to 1 if a member of the individual's household received financial assistance, such as payments from an old age or war veteran's pension programme, etc. (*Social Remittances*).

The second stage of our analysis examines the employment creation by the newly self-employed, and then the correlates of their short-term survival in the first year of business. It is well-known that new entrepreneurs bear the highest risk of failure during their first few years of activity. Table 1 has already indicated that some 40% of individuals becoming self-employed in Albania, and 50% of those in BiH quit their new entrepreneurial venture during their first year of activity[7]. We define two variables, namely *Employment Generation*, taking the value 1 if the individual is a newly self-employed that employs other individuals in his/her business, 2 if own-account self-employed, and 3 if the individual did not enter self-employment in 2002-2004. In similar spirit, we define *Business Survival* as a variable taking the value 1 if the individual remained in business one year upon entry, 2 if the individual failed in business during the first year, and 3 if the individual did not enter self-employment. We model employment creation and business survival in the multinomial probit framework, with individuals not self-employed as the comparison group. The set of explanatory variables is the same as in the previous section. Although firm and sector-specific determinants are also of vital importance, the nature of the database only enables individual-specific analysis. Primary interest in the survival equation is given to the relationship with human capital, labor market origins and access to finance (Holtz-Eakin et al., 1994; Cooper et al., 1994; Cressy, 1996; Astebro and Bernhardt, 2003).

[7] Observations of an individual in self-employment for two consecutive years do not necessarily establish survival in the same entrepreneurial activity. In order to ensure that survival in self-employment is captured we consider as "survivors", individuals declaring their status as self-employed in at least two consecutive years and with activity tenure more than a year in the second year of observation.

5. The Transition to Self-Employment

Table 3 introduces the variables that will be used in the analysis, along with summary statistics and mean differences between the newly self-employed and those that did not become self-employed. With respect to the socioeconomic profile of the newly self-employed, in all three countries, the newly self-employed is more likely to be male, urban region resident, with at least some level of secondary education, and another self-employed individual in the family. 65%-70% of the transitions in all three countries are by the male. While attitudes to risk are an important factor in determining such decision, this large difference between the sexes also shows that the women have fewer chances in the labor market. The demographic profile of the newly self-employed is more similar between Albania and BiH. In contrast, the newly self-employed in Serbia tend to be younger and less likely to be married compared to their non self-employed counterparts. Theory on the behavioral patterns of entrepreneurs stresses that the psychological profile and sociological background of individuals are important factors in the decision to initiate one's own business. The literature stresses the impact of social capital and optimism/overconfidence in particular. The data allows the construction of two proxies, for optimism and social capital considerations[8]. The newly self-employed in Albania and BiH are more likely to be optimistic about the future, and less likely to lack in terms of support from social capital.

An important branch of the literature has examined the links between wealth and entrepreneurship. The existence of borrowing constraints implies that own wealth and personal assets will be positively related to the propensity of individuals to engage in entrepreneurial activities (Evans and Jovanovic 1989; Paulson and Townsend, 2004). The summary statistics in Table 3 suggest that the new entrants into self-employment are less likely to be financially constrained in all three countries, in terms of wealth prior to entry. While there is significant evidence on the positive impact of wealth on entrepreneurial activity, empirical evidence on the role of financial institutions is relatively scarce. We utilize household affiliation with particular financial institutions and sources of finance in the

[8] We construct a proxy for social capital considerations, (*No Social Capital*) using the average of two available questions: (i) "Is there anyone you can count on to listen to you when you need to talk?", and (ii) "Is there anyone who you can really count on to help you out in a crisis?" These variables proxy for social capital in terms of the help people can get from friends, neighbors and relatives. A second dummy variable approximates *Optimism* in terms of financial expectations in terms of the future. These variables are not used in the regressions of the next section to avoid collinearity with other terms, such as wealth and education.

past and examine their relationship with the likelihood of starting a new business. The role of financial institutions is of particular interest in transition economies where the financial sector has undergone major reforms.

[Insert Table 3 about here]

The statistics in Table 3 suggest that the newly self-employed in Albania are less likely to have received informal finance, either in the form of a loan or as domestic remittances that they do not have to repay. They are also more likely to have obtained a loan from a micro-credit institution, although the fractions of the population that have obtained such a loan are small, i.e. 1.3% of the newly self-employed and 0.2% of their comparison group. In BiH, the newly self-employed are less likely to have received remittances from abroad and some type of social assistance, while in Serbia, there are no significant differences in the means of the financial institution variables. Moreover, the amount of remittances received in the past, both in currency units and a fraction of household consumption, is smaller for the newly self-employed compared to non-entrants.

Past employment experience has been shown to exert significant effects on current employment status. An important issue is related to informal sector experience and its relationship to entry into formal self employment. The relationship between the two is debatable, and the arguments are discussed in detail in Demirgüç-Kunt et al. (2009). In brief, this relationship could be expected to be either negative or positive, depending on whether informal markets should be viewed as the disadvantaged segment of a dual labor market that provides a subsistence shelter for unmatched employees (Harris and Todaro, 1970), or a competitive "grey economy" where heterogeneous entrepreneurs and workers weigh formal versus informal operation based on the cost of formal entry and the relative efficiency of formal and informal credit mechanisms and their related institutional arrangements (Maloney, 1999; Straub, 2005; *inter alia*). In economies under transition, the regulatory environment might not foster formal entrepreneurship and entrepreneurial individuals might choose to operate in the informal sector or shadow economy. Indeed, Djankov and Murrell (2002) document the existence of significant entry costs into formality, in the form of registration and license fees. The summary statistics in Table 3 indicate that individuals with experience in the informal sector are more likely to enter formal self-employment in all three countries, and a third of

the new entries are individuals with prior experience in "grey markets". In all three countries, the newly self-employed are less likely to come from unemployment-inactivity.

5.1 The Correlates of Self-Employment Entry

We model the decision to become self-employed in the probit framework, excluding individuals already self-employed in the beginning of each panel. The list of explanatory variables involves the standard correlates of self-employment activity in the literature. Moreover, in separate specifications, we examine the impact of household financial wealth, the relationship with financial institutions, as well as the role of labour market experience and origins. Interaction effects between these variables are also examined.

Table 4 presents our two baseline specifications for self-employment entry in Albania, BiH and Serbia separately. *Specification 1* incorporates the standard socioeconomic variables, while *specification 2* adheres the wealth proxy. Marginal effects and robust z-statistics of the coefficients are reported in absolute values. Standard errors were clustered at the household level, to correct for intra-household correlations.

[Insert Table 4 about here]

The results for Albania in Table 4 are consistent with the earlier differences in the means. The newly self-employed is more likely to be male, aged 38, residing in an urban area, married, with some formal education, in good health, and with another self-employed member in the household. The inclusion of the household consumption variable in *Column 2* indicates a significant positive effect of past wealth on current self-employment. This suggests that self-employed are more likely to rely on their own financial means in making their decision. The results from the same sets of estimates for BiH are consistent with Demirguc-Kunt et al. (2009). The newly self-employed are more likely to be male, in their early 40s, married, with some formal education, and in good health. The inclusion of the household consumption variable in *Column 2* indicates a significant positive effect of past wealth on current self-employment. The magnitude of the coefficient is greater than that for Albania. Finally, the last two columns of Table 4 present the estimation results for the 2003 self-employment

entries in the Serbian LSMS panel, suggesting these are more likely to be by male and urban area residents. The wealth proxy is of a smaller magnitude and marginally insignificant for Serbia.

Table 5 examines the impact of past employment experience in the three countries in our sample. The results indicate that ceteris paribus, informal sector employees are almost twice as likely to enter self-employment compared to employees in paid employment. The magnitude of the effect is very similar in the three countries, and is robust to the inclusion of the wealth variable in the specification. Furthermore, individuals employed abroad are less likely to start their own business in Albania during the sample time. Individuals coming from unemployment-inactivity are the ones least likely to start their own business in BiH. Column 3 further distinguishes between the presence of wage arrears among formal sector employees to allow for the potential of necessity entrepreneurship among formal sector employees. The results contradict this view in Albania and BiH, as employees receiving wage arrears are significantly less likely to make the transition to self-employment ceteris paribus, compared to employees receiving unusual or delayed payments. The difference between the two groups is insignificant in the Serbian sample.

[Insert Table 5 about here]

The positive coefficient for informal sector experience can be interpreted both in favour of the necessity-based "push" to self-employment, and/or the latent entrepreneur "pulling". While the persistence of the pattern both with and without the inclusion of the household income proxy favours the latter view, some further clarifications are needed on this interpretation. In order to shed some more light into the necessity versus opportunity/motivation discussion, we plot the predicted probabilities of entry by labor market status, versus (a) age and (b) household wealth decile, in Figure 4. It is evident in both plots that ceteris paribus, informal sector employees are the group that is most likely to enter formal self-employment at most ages and wealth levels. The latter probability is increasing in wealth level for all groups and countries. If informal sector employees enter formal self-employment due to necessity, then one would expect their entry profile to by non-linear in wealth. Thus, the evidence is more suggestive of a different explanation than necessity.

[Insert Figure 4 about here]

5.2 Self-Employment Entry and Access to Finance

Table 6 examines the relationship between self-employment entry and affiliation with financial institutions, along with informal sources of finance. Departing from the baseline specification, three specifications are implemented. In *Column (1)* the financial variables are added to the baseline specification. *Column (2)* incorporates household consumption along with the financial indicators, and *Column (3)* controls for labor market experience.

The estimation results for the three countries indicate that the decision to become an entrepreneur is unrelated to an existing relationship with formal financial institutions, confirming that these institutions rarely finance entry into self-employment. We fail to see a positive effect of formal microfinance institutions. However, there is also a significant negative effect by informal loans on the decision to start a new business in Albania and Serbia. However, remittances from abroad exhibit a significantly negative effect on the probability of an individual becoming self-employed in BiH, in accordance with the "disincentive effects" of remittances noted in the literature. This effect is economically significant, *i.e.* an individual switching from receiving money to not getting remittances has a 1.7% lower probability to become self-employed (almost 40% less likely). To the contrary, the impact of remittance receivership is statistically insignificant in Albania, where the incidence of remittance receivership is much higher. Transfers from institutional sources, such as charities and potentially international NGO initiatives have a positive impact on the probability to become self-employed in BiH. This result is economically large, although the use of these products is small in the overall sample (about 2% of individuals in our sample), which reduces the importance of this effect. These results hold with the inclusion of the wealth proxy and the labor origin variables.

[Insert Table 6 about here]

An important aspect of the situation in the Western Balkans, worthy of further attention, is related to remittance receivership. In Table 6, remittances from abroad are negatively associated with the probability of an individual becoming self-employed in Albania, and exert an insignificant impact in the other two countries. However, it is likely that the relationship between entry and remittance receivership is non-linear. In order to shed some more light into this issue, we examine the

relationship between entry and the amount of remittances received as a fraction of household income. In *Column 1* of Table 7 a new variable is introduced in the baseline specification, capturing the amount of remittances from abroad as a fraction of the household income proxy. A dummy for individuals not receiving foreign remittances is also introduced. The estimation results verify that individuals not receiving remittances are more likely to enter self-employment in BiH. However, controlling for foreign remittance receivership, the amount of remittances received as a fraction of household consumption is not significantly associated with entry in the three countries.

[Insert Table 7 about here]

Figure 5 plots the predicted probability of entry in each country versus the ratio of foreign remittances to equivalized household consumption. The figures indicate a negative association between the volume of remittances received as a fraction of per capital consumption and the probability of entry in Albania, and a more U-shaped profile of this relationship for BiH and Serbia.

[Insert Figure 5 about here]

Finally, Table 8 presents estimates of the interaction effects between labor market origins and access to finance, allowing for some additional heterogeneity in the relationship between access to finance and entry. The intuition of this exercise is to explore the relationship of labor market status and the provision of access to (in)formal sources of finance. Importantly, the probit models with the interactions between financial and labor market variables are estimated in the framework proposed by Ai and Norton (2003) and Norton, Wang and Ai (2004) for interaction effects in non-linear models. The specifications are all similar to *Column 1* of Table 4, plus the two variables to be interacted and the interaction term. An interesting difference comes up with respect to the utilization of remittances from abroad in Albania. The interaction effect between remittances and informal sector employment is positive. In contrast, the interaction between remittances and formal sector employment exhibits a negative effect. This may suggests that remittances from abroad cover for the absence of formal financing mechanisms for individuals less likely to gain access to formal finance, such as those in the informal sector. A summary of the interaction terms for BiH suggests a positive interaction between microcredit schemes and informal sector employment. Informal sector employees provided with a micro-loan are significantly more likely to start their own business. This

is not the case with formal sector employees and those not previously employed, none of which is observed to become self-employed when provided with a loan from a micro-credit scheme. Furthermore, interactions between formal means of finance and labor origins suggest a positive effect of the interaction term between bank loans and unemployment/inactivity. The interaction effects for Serbia suggest a positive interaction between informality and wealth in the decision to start a new business.

[Insert Table 8 about here]

5.3 Self-Employment Performance

It has already been established that the three countries have their own particularities when it comes to business operation. Specifically, the country ranks particularly low in the easy of employing workers in World Bank's "Doing Business" Indicators, and as it was shown, almost half of the new businesses do not make it through their first year in business. Moreover, the results so far suggest two main patterns that appear robust across the three countries and specifications. First, experience into informal markets is positively related to later self-employment, and second, affiliation with institutions providing formal finance is not significantly associated to entry. In this section, we extend the analysis to the correlates of employment creation and business survival.

In particular, in Table 9 we show results from a multinomial probit model, where the dependent variable takes the value if the individual switches to self-employment with employees (*Employer*), the value 2 if the individual switches to self-employment without employees (*Own-Account*), and the value 3 if the individual does not switch to self-employment. An advantage of this model is that it is free of the restrictive Independence of Irrelevant Alternatives Assumption (IIA), without requiring identification restrictions. It has been used in the past to examine self-employment survival by Djankov et al. (2006a). The results are consistent with the previous tables. However, there are some interesting differences. Bank loan affiliation is associated with employment creation upon entering self-employment in BiH. Reasonably, larger firms require greater up-front capital. Moreover, informal sources of finance, such as informal loans and remittances from abroad are less likely to be related to large-scale start ups. Finally, employees from the informal sector are more likely to start as

own account self-employed in BiH, and appear in both the employer and own-account categories in Serbia.

[Insert Table 9 about here]

In Table 10, we examine the post-entry performance of the newly self-employed individuals. The dependent variable takes the value 1 if the individual was still in business in the year following entry (*Survivor*). It takes the value 2 if the individual failed during his/her first year in business (*Failed*) and 3 if the individual did not enter self-employment during sample lifetime. The year coverage of the panels for Albania and BiH allows this operation. It has already been mentioned that some 40%-50% of the newly self-employed in Albania and almost half in BiH fail during their first year in business. It is thus of interest to examine the relationship between individual characteristics such as those prior to entry and the viability of the new business attempts. Marginal effects and robust z-statistics are presented.

The results in Table 10 suggest that the male, the older, urban area residents, those with another self-employed member in the household and greater own wealth have higher chances of survival in business, for at least one year. Interestingly, individuals coming from the informal sector also exhibit higher chances of survival. The results suggest that older people, those with another self-employed in the household, and individuals with greater social capital have slightly better chances of success. Informal means of finance, such as domestic remittances, remittances from abroad and social assistance money bring lower chances of success. Bank financing is associated with greater survival chances in BiH.

[Insert Table 10 about here]

6. Conclusion

This chapter examines and discusses the correlates of new entry into self-employment in three neighboring Balkan countries, i.e. Albania, Bosnia and Herzegovina, and Serbia. It makes use of the *World Bank Living Standard Measurement Survey Data* available for the region and extends the analysis in

Demirguc-Kunt et al. (2009) for the role of labor market experience and access to finance. All three countries are in the long difficult path of transition after multiple shocks in the 1990s and have gone through major reform processes with the aim to improve the labor and business environment. The promotion of micro-enterprise activity has been a key political priority in the region in recent years, as the rates of self-employment and new business entry are still among the lowest in the three countries among transition economies.

Among the primary findings, informal sector employees are the ones more likely to make the transition to formal self-employment. This is a result that is quite robust, for both genders, excluding farmers etc. In support of this finding, is the positive interaction effect between informality and access to finance through microloans and informal sources of finance, such as remittances from abroad. Informal sector employees are also the ones more likely to survive the first year in business. This finding is in accordance with the financed-based, competitive view of informality, suggesting that credit constraints are the driving force behind it. Moreover, it can be linked to a number of arguments, such as: (a) Lazear's (2004) view of entrepreneurs as "jacks of all trades"; (b) the human capital acquisition and skills transferability literature (Guariglia and Kim, 2006; *inter alia*), and (c) Baumol's (1990) idea of a fixed pool of entrepreneurial talent. In the latter case, the increase in the number of self-employed could conform with the reallocation of that talent in more efficient markets. It is of great further interest to examine if this pattern persists in regression analysis that accounts for household income and other characteristics.

The informal sector in the Western Balkans can be viewed as incubator of new entries into formal self-employment by otherwise potentially skilled and entrepreneurial workers who might prefer to stay informal until the institutional environment allows better conditions. This feature indicates that it is not so much the lack of entrepreneurial spirit that contributes to the poor labor market environment, as the lack of regulation and motivation to operate formally. A potential link between informal experience and later formal entry has important policy implications (Kaufmann & Kaliberda, 1996; Johnson et al., 1997). The most prominent implication shifts the focus from the banning of informality to the operation of the financial market and the provision of incentives for employment growth and viability.

Moreover, wealthier households are more likely to become entrepreneurs and survive the early period in business, emphasizing the importance of internal finance. Variables indicating financial institution customer affiliation, in terms of loans from formal financial institutions, or even informal sources that one needs to repay, have insignificant impact on self-employment transitions. However, an existing prior relationship with a bank is related the chances of survival for new entrepreneurs, suggesting that while banks rarely finance entry decisions, they are still instrumental in survival. Informal finance on the other hand is negatively associates with employment creation. The results highlight that the three Western Balkan neighbors still have some road in that transition process.

The importance of external finance by formal institutions can have the desirable impact on private sector development, only after property rights are established and well-defined, in order to provide an essential level of security in a stable macroeconomic environment. Even after reforms are introduced, establishing appropriate norms and sets of incentives to nascent entrepreneurs requires a longer horizon. Given the fact that in the transition countries of Eastern and Central Europe, the small and medium enterprise (SME) sector has been an important creator of new jobs, it is evident that the provision of incentives to operate formally should be a key policy incentive in the three Western Balkan countries in this chapter. The creation of an environment that promotes formal self-employment is essential for employment creation, the reduction of informal operations, and should ultimately be a target that could promote sustainable growth in the region.

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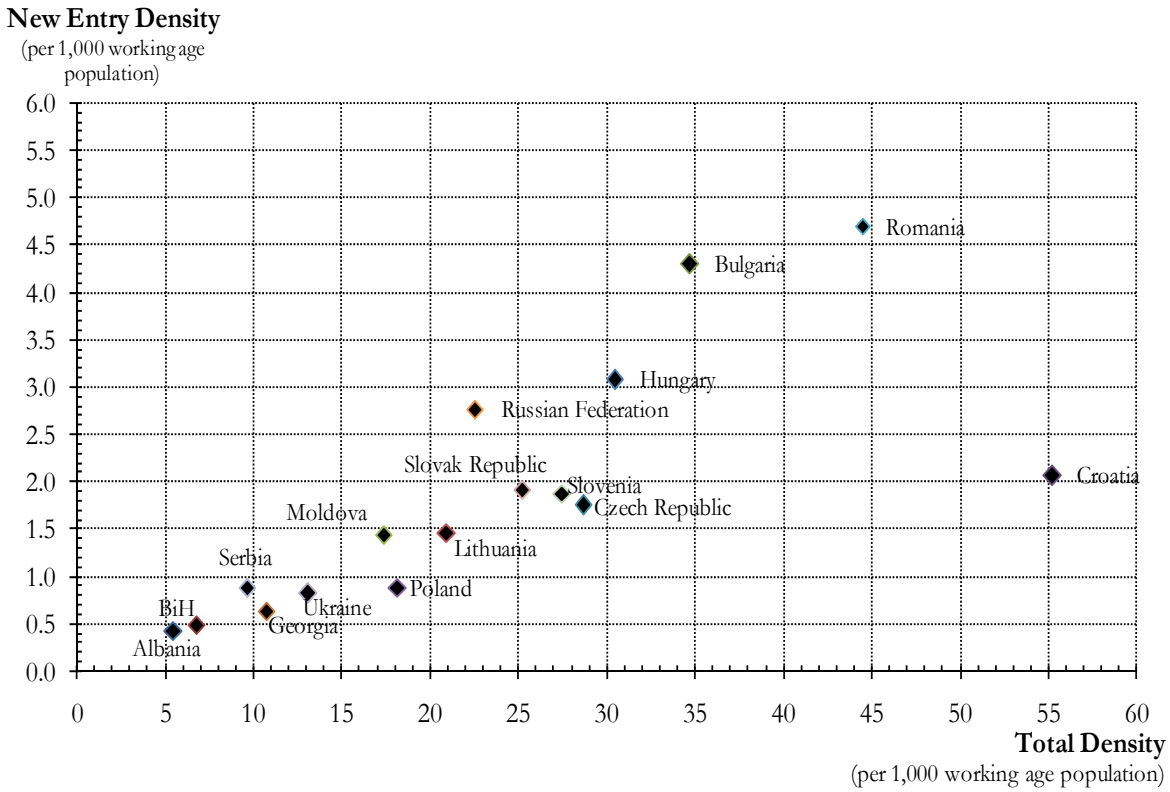
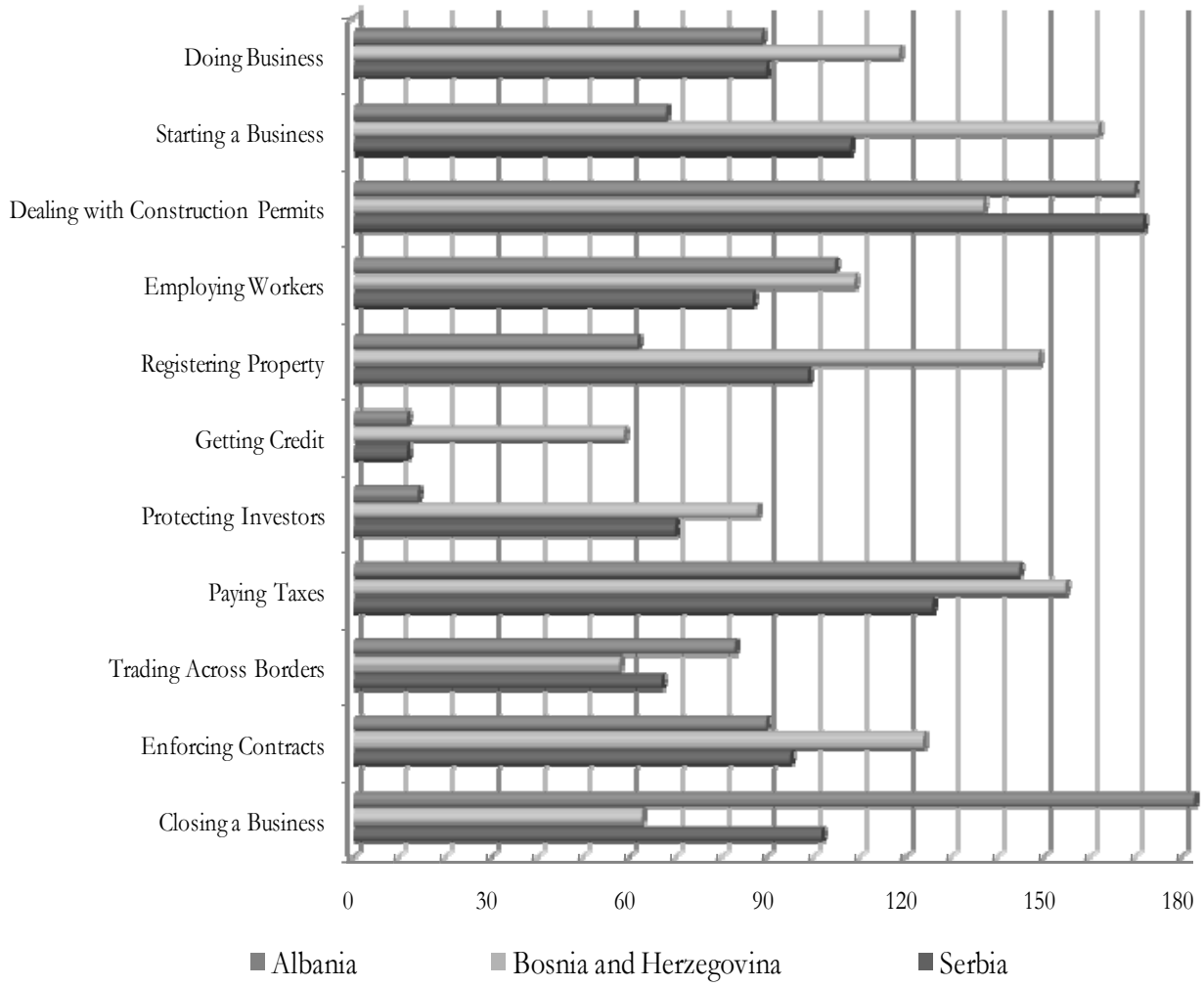
Figure 1
Overall Business and New Entry Density is ECE



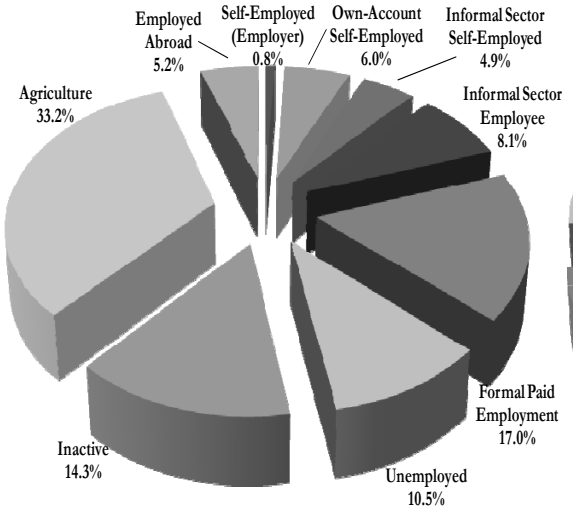
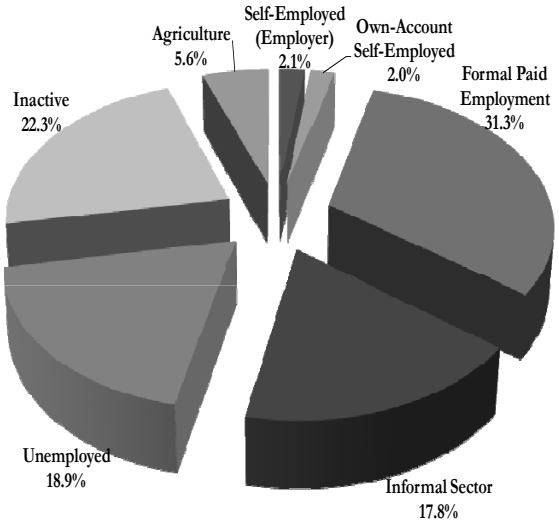
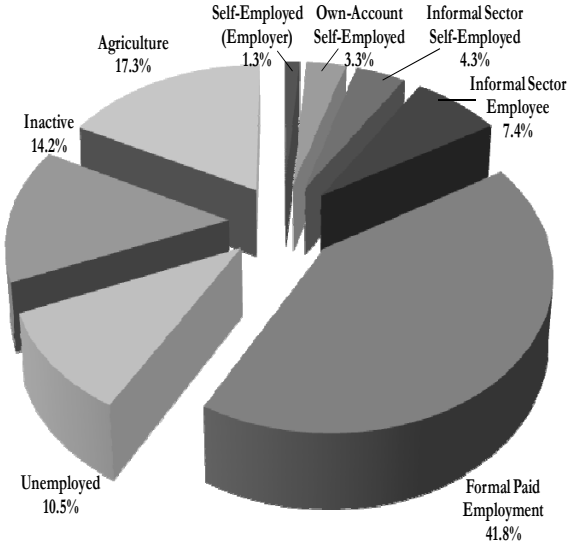
Source:
World Bank Group 2008 Entrepreneurship Database (2002-2004 averages)
http://rru.worldbank.org/businessplanet/default.aspx?pid=8

Figure 2
Ease of Doing Business Ranking in Albania, Bosnia & Herzegovina, and Serbia



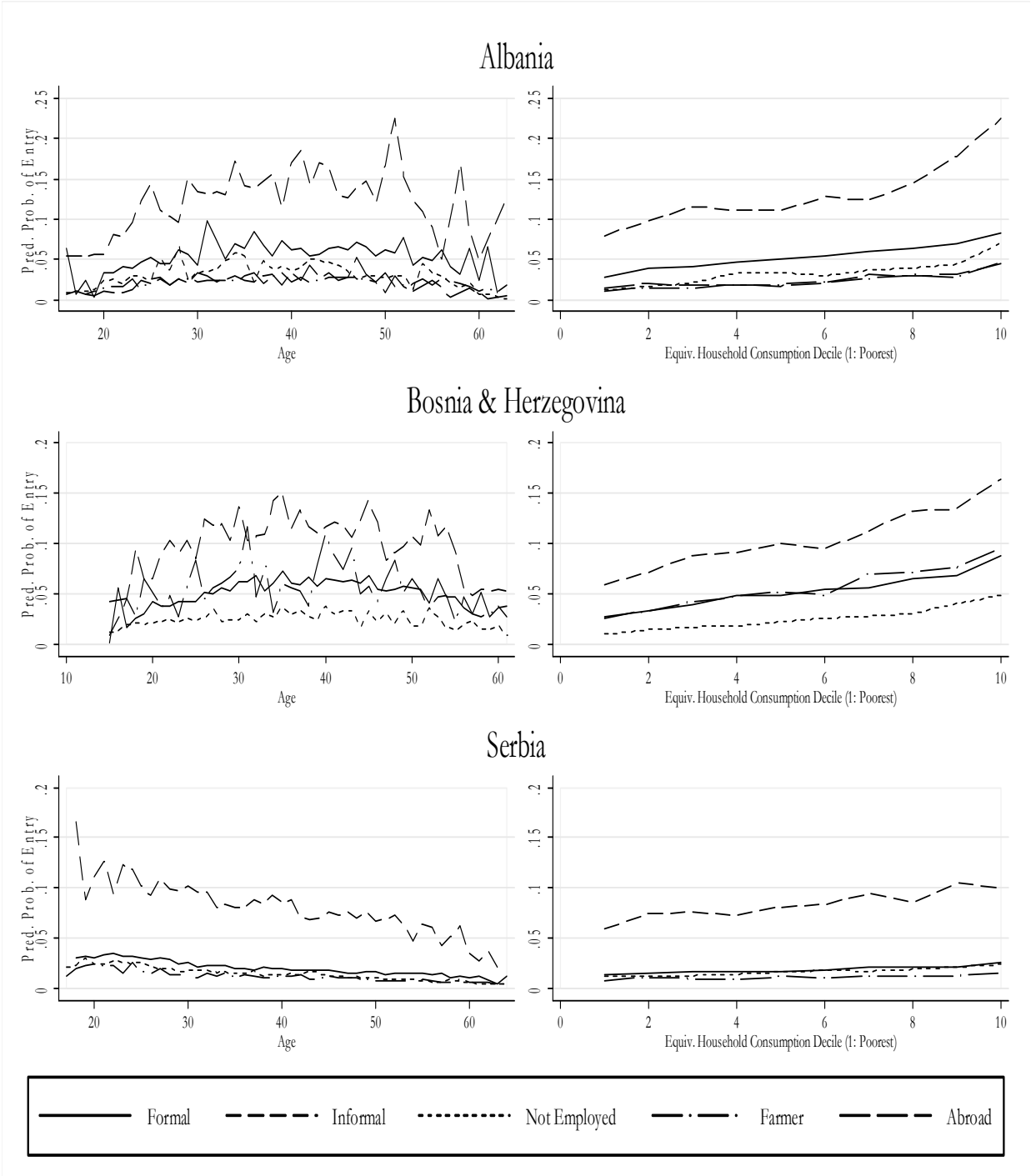
Source:
World Bank Group Doing Business Indicators (2009; Total of 183 countries).
http://rru.worldbank.org/businessplanet/default.aspx?pid=1

Figure 3
Labor Force Composition in Albania, Bosnia & Herzegovina, and Serbia

Albania	**Bosnia & Herzegovina**	**Serbia**
World Bank LSMS (2002-2004)	World Bank LSMS (2001-2004)	World Bank LSMS (2002-2003)
		
Sample Averages for 2002-2004	*Sample Averages for 2001-2004*	*Sample Averages for 2002-2003*
(10,650 Observations; 3,550 Individuals)	*(19,088 Observations; 4,772 Individuals)*	*(7,146 Observations; 3,708 Individuals)*

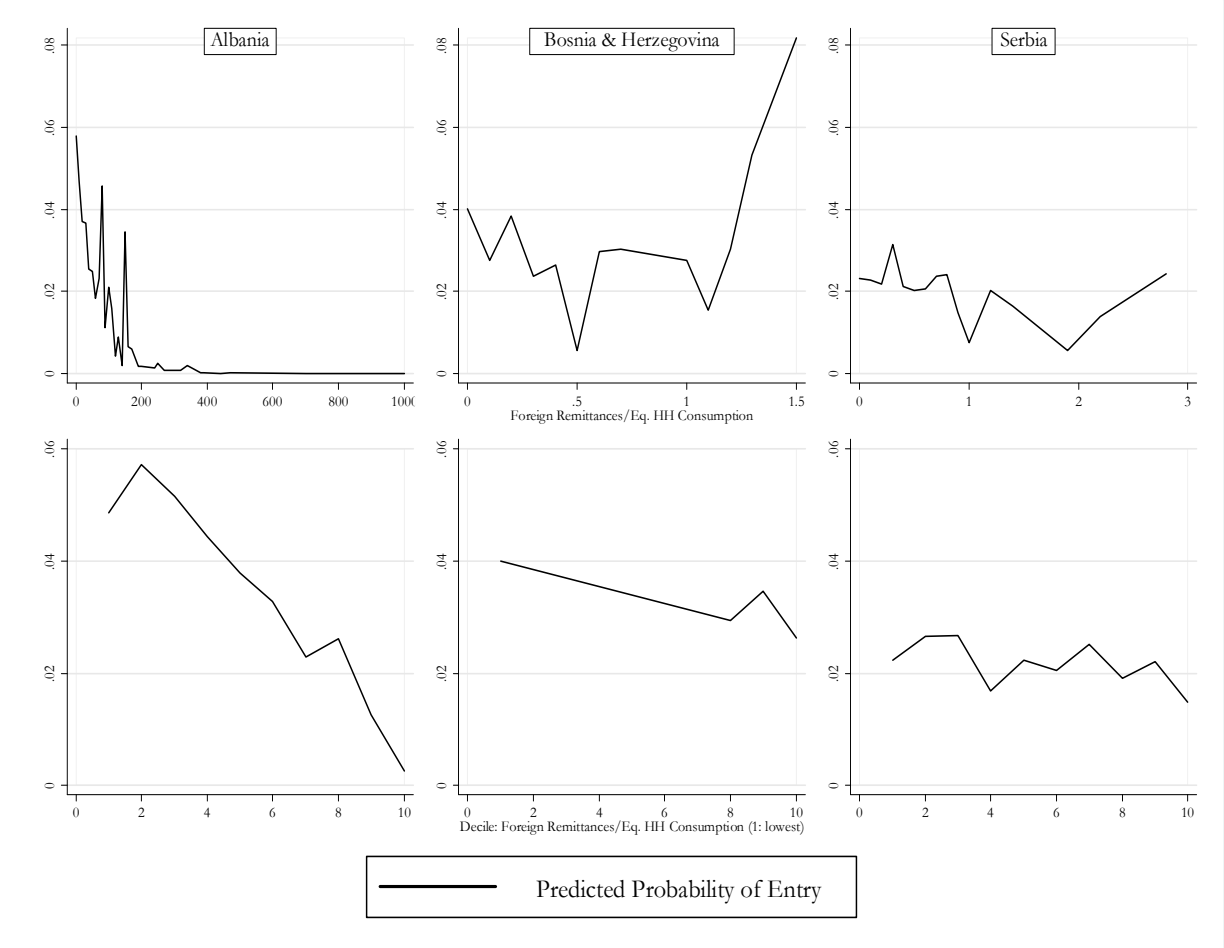
Notes:
The distinction between formally and informally self-employed in Albania can be made based on the tax records of businesses in Wave 1. This distinction can not be made in Bosnia, but the informal sector category apparently contains both self-employed and employees.

Figure 4
Entry Probability by Labor Market Status



Notes: Predicted Probabilities are from specification (2) of Table 5. The category "Employed Abroad" only exists in Albania.

Figure 5
Entry and Remittance Receivership



Notes: Predicted Probabilities are from specification (2) of Table 7

Table 1
New Self-Employment Entry
World Bank Living Standards Measurement Surveys (LSMS)

	Albania		Bosnia & Herzegovina		Serbia	
	Individuals	HH Heads	Individuals	HH Heads	Individuals	HH Heads
New Entry						
2001	-	-	-	-	-	-
2002	-	-	107	49	-	-
2003	98	49	71	37	88	38
2004	58	25	44	24	-	-
Total	156	74	222	110	88	38
Employment Generation						
Employers	7	4	83	34	23	15
Own-Account	149	70	139	76	65	23
Survival in:	2003		2002-2003		-	
Survivors	58	29	91	41	-	-
Failed	40	20	87	45	-	-

Notes: The figures are for individuals that were not self-employed in the beginning of the panels

Table 2
Labour Market Status and Individual Welfare
World Bank Living Standards Measurement Surveys (LSMS)

	Equiv. Household Consumption Decile			Life Satisfaction (1-7)		Economic Status Assessment (1-10)	HH Income Satisfaction (1-7)	Financial Status (1-4)	
	Albania	*BiH*	*Serbia*	*Albania*	*BiH*	*Albania*	*BiH*	*Albania*	*Serbia*
Self-Employed:									
Employer	8.71	7.43	8.27	5.41	5.17	6.71	4.60	2.93	2.97
Own-Account	7.10	6.96	6.28	4.51	4.64	5.35	3.92	2.25	2.55
Formal Paid Employment	6.41	6.33	5.80	4.28	4.81	4.16	3.76	1.95	2.42
Informal Sector:									
Self-Employed	6.09	5.49	5.47	3.58	4.28	4.00	3.17	1.77	2.37
Employee	5.23		5.28	3.49		3.81		1.73	2.30
Unemployed	4.27	4.60	4.46	3.38	4.14	3.02	2.62	1.50	1.96
Inactive	5.11	5.50	4.53	3.47	4.55	3.55	3.25	1.70	2.24
Agriculture	4.31	5.84	4.74	3.53	4.47	3.31	3.40	1.77	2.36
Employed Abroad	4.55	-	-	3.81	-	3.28	-	1.80	-

Table 3
Sample averages and mean differences

	Albania			Bosnia & Herzegovina			Serbia		
	Pooled	*Entry*	*No Entry*	*Pooled*	*Entry*	*No Entry*	*Pooled*	*Entry*	*No Entry*
	(3,293)	(156)	(3,137)	(4,538)	(222)	(4,316)	(3,708)	(88)	(3,620)
Individual and Household Characteristics:									
Male	47.6%	69.2%***	46.5%	51.5%	68.0%***	50.7%	51.5%	64.8%**	51.1%
Age	36.4	38.6**	36.3	35.9	37.3*	35.8	40.67	37.4	40.7***
Married/Cohabiting	76.6%	84.6%**	76.2%	62.1%	74.8%***	61.5%	74.9%	67.1%	75.1%*
Number of Children	1.12	1.24	1.11	1.39	1.47	1.38	1.34	1.24	1.34
Federation of BiH	-	-	-	54.7%	49.6%	54.9%	-	-	-
Urban region	43.0%	65.4%***	41.9%	42.8%	50.0%**	42.5%	56.6%	68.2%**	56.3%
Low Education	63.7%	38.5%	65.0%***	34.1%	22.1%	34.7%***	32.7%	21.6%	33.0%**
Disabled/Chronic ill.	6.4%	1.9%	6.6%**	5.2%	2.7%	5.3%*	7.0%	9.1%	7.0%
Another S.E. family member	3.0%	12.2%***	2.5%	6.5%	16.7%***	6.0%	4.6%	8.0%	4.5%
Optimism	29.2%	38.5%***	28.7%	26.6%	32.4%**	26.3%	-	-	-
No Social Capital	5.4%	3.2%	5.6%	11.0%	4.5%	11.3%***	-	-	-
Wealth and Financial Characteristics:									
Equivalized Household Consumption	9,152	11,101***	9,055	2,713	3,318***	2,681	79,294	91,912**	78,986
Property Owner	93.2%	91.0%	93.3%	69.6%	70.7%	69.6%	89.4%	94.3%	89.3%
Informal Loan	13.0%	7.7%	13.2%**	17.2%	15.3%	17.3%	4.5%	1.1%	4.5%
Micro Loan	0.3%	1.3%**	0.2%	2.6%	2.7%	2.6%	-	-	-
Bank Loan	0.9%	1.3%	0.9%	11.8%	12.6%	11.7%	5.6%	4.6%	5.6%
Domestic Remittances	11.8%	5.1%	12.1%***	8.2%	5.4%	8.3%	6.9%	4.6%	6.9%
Remittances from Abroad	32.4%	32.7%	32.4%	11.9%	7.2%	12.1%**	6.5%	5.7%	6.5%
Amount of foreign remittances‡	272,348	81,725	281,925**	978	491	992*	28,939	22,000	29,086*
Foreign Remit./HH Consumption‡	32.55	8.14	33.78**	0.443	0.156	0.452*	0.369	0.315	0.370
NGO/Charity/Grant money	6.1%	4.5%	6.2%	1.8%	2.7%	1.8%	3.0%	2.3%	3.0%
Humanitarian help/Social institutions	23.6%	16.0%	23.9%**	26.2%	20.7%	26.5%*	22.0%	21.6%	22.0%
Labour Market Characteristics:									
Formal Sector Employee	20.3%	26.3%*	20.0%	35.9%	40.1%	35.7%	42.9%	35.2%	43.1%
… not in Wage Arrears	11.1%	16.7%**	10.8%	23.6%	30.3%**	23.3%	34.0%	30.7%	34.1%
Informal Sector	13.6%	38.5%***	12.4%	14.7%	32.0%***	13.8%	11.7%	40.9%***	11.0%
Unemployed/Inactive	24.7%	16.7%	25.1%**	43.6%	21.6%	44.7%***	23.8%	15.9%	24.0%*
Agriculture	36.4%	16.0%	37.5%***	5.8%	6.3%	5.8%	16.8%	8.0%	17.0%**
Employed Abroad	5.0%	2.6%	5.1%	-	-	-	-	-	-

Notes:
* p<0.10, ** p<0.05, *** p<0.01
‡ These two figures for the amount of remittances are among remittance receivers only.
The national currencies at the time of the survey were:
Albania: *Albanian Lek*. The exchange rate in November 2001 was 140.16 Leke per 1 $US.
Bosnia & Herzegovina: *Konvertibilna Marka* (convertible mark or BAM), introduced in 1998 initially pegged to the German Deutsch Mark and later to the. euro. In 2002, the currency was put on a fixed exchange rate of 1 BAM to €0.511292 euro (€1 = 1.95583 BAM). The relationship to the dollar was: 2001: 2.1857 BAM per $US,2002-2003: 1.7329 BAM per $US.
Serbia: *New Yugoslav Dinar*. The exchange rate in January 2002 was 65 new Yugoslav dinars per $US 1.

Table 4
Self-employment Entry

	Albania		Bosnia & Herzegovina		Serbia	
	(1)	(2)	(1)	(2)	(1)	(2)
Male	0.038***	0.039***	0.034***	0.035***	0.013***	0.013***
	[5.93]	[6.04]	[5.70]	[5.98]	[2.67]	[2.68]
Age	0.006***	0.006***	0.006***	0.005***	0.0005	0.0003
	[3.04]	[3.02]	[3.36]	[3.25]	[0.28]	[0.18]
Age squared/1,000	-0.080***	-0.081***	-0.074***	-0.073***	-0.014	-0.012
	[3.17]	[3.23]	[3.31]	[3.41]	[0.64]	[0.55]
Married/Cohabiting	0.007	0.009	0.022**	0.021**	0.002	0.002
	[0.76]	[0.98]	[2.30]	[2.38]	[0.28]	[0.22]
Log(Number of Children)	0.006**	0.005**	-0.005	0.002	-0.004	-0.003
	[2.43]	[2.23]	[0.61]	[0.19]	[0.92]	[0.71]
Federation of Bosnia & Herzegovina	-	-	-0.008	-0.009	-	-
			[1.22]	[1.45]		
Urban region	0.022***	0.019***	0.009	0.006	0.010**	0.010*
	[2.95]	[2.58]	[1.36]	[0.96]	[1.96]	[1.85]
Low Education	-0.026***	-0.021***	-0.016**	-0.011*	-0.005	-0.003
	[3.21]	[2.63]	[2.53]	[1.81]	[0.84]	[0.56]
Disabled	-0.021**	-0.020**	-0.025***	-0.023***	0.011	0.008
	[2.36]	[2.25]	[3.23]	[2.96]	[0.79]	[0.63]
Another self-employed member in the family	0.146***	0.131***	0.089***	0.073***	0.012	0.010
	[3.66]	[3.43]	[3.83]	[3.54]	[0.87]	[0.78]
Log(Equivalized Household Consumption)	-	0.015**	-	0.030***	-	0.007
		[2.18]		[4.95]		[1.47]
Observed Probability	0.0474	0.0474	0.0489	0.0490	0.0249	0.0249
Predicted Probability	0.0322	0.0314	0.0394	0.0371	0.0219	0.0217
Derivative Adjustment Factor	0.0312	0.0304	0.0378	0.0357	0.0214	0.0212
Number of Entries	156	156	222	222	88	88
Number of observations	3,293	3,293	4,538	4,531	3,531	3,531
Pseudo R^2	0.109	0.113	0.065	0.080	0.031	0.034
Log-Likelihood	-559.8	-556.9	-828.7	-814.8	-399.2	-398.0
Wald χ^2	110.4***	116.7***	111.0***	124.5***	30.2***	30.9***

Notes:
Dependent variable: Newly Self-Employed (1/0): Probit regressions; Marginal Effects and robust z-statistics (absolute values) are presented in brackets. Standard errors are clustered at the household level. The difference in the predicted value for discrete changes (0-1) is reported for the dummy variables. For continuous variables, the derivatives of the predicted dependent variable for small changes in the exogenous variables are reported.

Table 5
Self-employment Entry and Labor Market Experience

	Albania			Bosnia & Herzegovina			Serbia		
	(1)	(2)	(3)	(1)	(2)	(3)	(1)	(2)	(3)
Male	0.030***	0.031***	0.031***	0.025***	0.027***	0.027***	0.008*	0.008*	0.008*
	[4.57]	[4.68]	[4.74]	[4.46]	[4.83]	[4.93]	[1.85]	[1.87]	[1.89]
Age	0.005**	0.005**	0.004**	0.004**	0.004**	0.004**	0.0001	-0.00001	0.00002
	[2.47]	[2.47]	[2.39]	[2.40]	[2.41]	[2.51]	[0.03]	[0.01]	[0.01]
Age squared/1,000	-0.063***	-0.063***	-0.061***	-0.054**	-0.056***	-0.058***	-0.008	-0.007	-0.007
	[2.60]	[2.67]	[2.59]	[2.43]	[2.61]	[2.72]	[0.38]	[0.34]	[0.36]
Married/Cohabiting	0.006	0.008	0.009	0.020**	0.020**	0.020**	0.002	0.001	0.001
	[0.76]	[0.97]	[1.07]	[2.27]	[2.39]	[2.44]	[0.28]	[0.23]	[0.22]
Log(Number of Children)	0.006***	0.005**	0.005**	-0.004	0.002	0.002	-0.005	-0.004	-0.004
	[2.58]	[2.37]	[2.34]	[0.52]	[0.23]	[0.25]	[1.12]	[0.94]	[0.94]
Federation of Bosnia & Herzegovina	-	-	-	-0.003	-0.005	-0.006	-	-	-
				[0.55]	[0.81]	[1.10]			
Urban region	0.011	0.010	0.009	0.011*	0.008	0.008	0.008	0.007	0.007
	[1.45]	[1.26]	[1.21]	[1.78]	[1.41]	[1.31]	[1.55]	[1.48]	[1.48]
Low Education	-0.027***	-0.023***	-0.023***	-0.019***	-0.015**	-0.015**	-0.003	-0.002	-0.002
	[3.40]	[2.88]	[2.96]	[3.07]	[2.49]	[2.53]	[0.48]	[0.31]	[0.28]
Disabled	-0.018**	-0.017*	-0.018**	-0.024***	-0.022***	-0.022***	0.012	0.01	0.01
	[1.99]	[1.91]	[2.08]	[3.52]	[3.23]	[3.26]	[0.90]	[0.78]	[0.78]
Another self-employed family member	0.115***	0.102***	0.099***	0.084***	0.069***	0.067***	0.011	0.01	0.01
	[3.07]	[2.88]	[2.86]	[3.80]	[3.50]	[3.47]	[0.88]	[0.83]	[0.82]
Log(Equiv. Household Consumption)	-	0.014**	0.015**	-	0.027***	0.027***	-	0.005	0.005
		[2.18]	[2.24]		[4.59]	[4.63]		[1.07]	[1.02]
Formal Sector*No Wage Arrears	-	-	0.022*	-	-	0.023**	-	-	0.009
			[1.68]			[2.01]			[0.84]
Informal sector	0.039**	0.041***	0.062***	0.047***	0.047***	0.074***	0.052***	0.052***	0.073**
	[2.55]	[2.64]	[2.62]	[3.92]	[3.98]	[3.70]	[3.75]	[3.76]	[2.43]
Unemployed/Inactive	-0.005	-0.003	0.008	-0.013*	-0.009	0.006	-0.003	-0.002	0.006
	[0.59]	[0.34]	[0.64]	[1.77]	[1.26]	[0.57]	[0.41]	[0.29]	[0.48]
Agriculture	-0.009	-0.007	0.003	0.029	0.028	0.053*	-0.004	-0.004	0.003
	[0.95]	[0.72]	[0.25]	[1.51]	[1.48]	[1.89]	[0.57]	[0.55]	[0.26]
Employed Abroad	-0.019**	-0.018**	-0.012	-	-	-	-	-	-
	[2.36]	[2.07]	[0.96]						
Observed Probability	0.0474	0.0474	0.0474	0.0489	0.0490	0.0490	0.0249	0.0249	0.0249
Predicted Probability	0.0301	0.0293	0.0290	0.0360	0.0341	0.0337	0.0185	0.0184	0.0183
Derivative Adjustment Factor	0.0292	0.0284	0.0282	0.0347	0.0329	0.0325	0.0181	0.0181	0.0179
Number of Entries	156	156	156	222	222	222	88	88	88
Number of observations	3,293	3,293	3,293	4,538	4,531	4,531	3,531	3,531	3,531
Pseudo R^2	0.133	0.138	0.14	0.09	0.104	0.107	0.081	0.083	0.084
Log-Likelihood	-544.5	-541.6	-540.2	-806.4	-794.0	-791.3	-378.2	-377.6	-377.2
Wald χ^2	133.5***	139.8***	142.1***	160.2***	176.0***	181.8***	82.8***	82.4***	86.8***

Notes: Comments in Table 4 apply.

Table 6
Self-employment Entry and Access to Finance

	Albania			Bosnia & Herzegovina			Serbia		
	(1)	(2)	(3)	(1)	(2)	(3)	(1)	(2)	(3)
Male	0.038***	0.038***	0.030***	0.034***	0.035***	0.025***	0.013***	0.013***	0.008*
	[5.93]	[6.03]	[4.60]	[5.74]	[6.02]	[4.53]	[2.74]	[2.76]	[1.87]
Age	0.006***	0.006***	0.004**	0.006***	0.005***	0.004**	0.0004	0.0002	-0.0001
	[3.02]	[2.99]	[2.43]	[3.31]	[3.23]	[2.38]	[0.24]	[0.12]	[0.04]
Age squared/1,000	-0.077***	-0.078***	-0.060**	-0.071***	-0.071***	-0.052**	-0.013	-0.01	-0.006
	[3.16]	[3.20]	[2.56]	[3.27]	[3.42]	[2.42]	[0.61]	[0.51]	[0.33]
Married/Cohabiting	0.006	0.008	0.006	0.022**	0.021**	0.020**	0.002	0.002	0.002
	[0.66]	[0.85]	[0.66]	[2.38]	[2.49]	[2.39]	[0.32]	[0.27]	[0.31]
Log(Number of Children)	0.005**	0.005**	0.005**	-0.005	0.002	-0.004	-0.005	-0.004	-0.005
	[2.09]	[2.00]	[2.32]	[0.57]	[0.30]	[0.49]	[1.06]	[0.91]	[1.21]
Federation of Bosnia & Herzegovina	-	-	-	-0.009	-0.011*	-0.005	-	-	-
				[1.48]	[1.71]	[0.85]			
Urban region	0.023***	0.020***	0.012	0.008	0.005	0.011*	0.011**	0.010**	0.008*
	[3.03]	[2.67]	[1.58]	[1.33]	[0.87]	[1.77]	[2.17]	[2.05]	[1.73]
Low Education	-0.022***	-0.019**	-0.024***	-0.016**	-0.011*	-0.019***	-0.005	-0.003	-0.003
	[2.90]	[2.43]	[3.17]	[2.53]	[1.79]	[3.13]	[0.84]	[0.56]	[0.46]
Disabled	-0.019**	-0.018**	-0.016*	-0.024***	-0.021***	-0.023***	0.012	0.009	0.013
	[2.10]	[2.02]	[1.72]	[2.95]	[2.67]	[3.29]	[0.87]	[0.69]	[0.96]
Another self-employed family member	0.141***	0.129***	0.111***	0.089***	0.072***	0.084***	0.013	0.011	0.012
	[3.61]	[3.40]	[3.07]	[3.79]	[3.48]	[3.75]	[0.96]	[0.85]	[0.94]
Log(Equivalized Household Consumption)	-	0.013*	-	-	0.031***	-	-	0.008*	-
		[1.77]			[5.20]			[1.65]	
Informal sector	-	-	0.040***	-	-	0.050***	-	-	0.050***
			[2.61]			[4.06]			[3.69]
Unemployed/Inactive	-	-	-0.004	-	-	-0.011	-	-	-0.003
			[0.47]			[1.58]			[0.52]
Agriculture	-	-	-0.008	-	-	0.031	-	-	-0.004
			[0.80]			[1.61]			[0.53]
Employed Abroad	-	-	-0.019**	-	-	-	-	-	-
			[2.28]						
Informal Loan	-0.023	-0.027*	-0.025*	-0.006	-0.007	-0.007	-0.018***	-0.018***	-0.015***
	[1.27]	[1.74]	[1.93]	[0.83]	[1.05]	[1.10]	[3.29]	[3.37]	[2.79]
Micro Loan	0.241	0.278	0.266	-0.003	-0.007	-0.009	-	-	-
	[0.81]	[0.88]	[0.93]	[0.19]	[0.46]	[0.71]			

Table 6 continued in next page

Table 6 continued from last page

Bank Loan	0.040	0.049	0.062	0.004	0.001	0.005	-0.006	-0.007	-0.005
	[0.62]	[0.69]	[0.88]	[0.42]	[0.14]	[0.52]	[0.68]	[0.77]	[0.64]
Domestic Remittances	0.02	0.035	0.027	-0.008	-0.007	-0.006	-0.007	-0.008	-0.007
	[0.43]	[0.61]	[0.62]	[0.84]	[0.70]	[0.66]	[0.88]	[1.02]	[1.19]
Remittances from Abroad	0.003	0.002	0.002	-0.017**	-0.018***	-0.017**	-0.002	-0.002	-0.001
	[0.45]	[0.30]	[0.31]	[2.29]	[2.60]	[2.42]	[0.16]	[0.22]	[0.05]
Institutional Remittances	-0.011	-0.01	-0.01	0.080*	0.098**	0.095**	-0.005	-0.004	-0.007
	[1.10]	[1.05]	[1.07]	[1.90]	[2.10]	[2.03]	[0.37]	[0.34]	[0.72]
Social Remittances	-0.012*	-0.009	-0.01	-0.005	-0.004	-0.005	0.004	0.006	0.003
	[1.74]	[1.30]	[1.46]	[0.76]	[0.64]	[0.80]	[0.61]	[0.80]	[0.54]
Observed Probability	0.0474	0.0474	0.0474	0.0489	0.0490	0.0489	0.0249	0.0249	0.0249
Predicted Probability	0.0312	0.0307	0.0292	0.0384	0.0360	0.0349	0.0210	0.0207	0.0177
Derivative Adjustment Factor	0.0303	0.0297	0.0283	0.0369	0.0347	0.0336	0.0206	0.0203	0.0174
Number of Entries	156	156	156	222	222	222	88	88	88
Number of observations	3,293	3,293	3,293	4,538	4,531	4,538	3,531	3,531	3,531
Pseudo R^2	0.116	0.119	0.140	0.072	0.089	0.099	0.038	0.041	0.088
Log-Likelihood	-555.3	-553.2	-540.4	-822.6	-807.5	-799	-396.3	-394.8	-375.6
Wald χ^2	116.2***	123.6***	140.1***	123.9***	136.3***	173.3***	40.3***	41.9***	102.3***

Notes: Comments in Table 4 apply.

Table 7
Self-employment Entry and Remittances from Abroad

	Albania		Bosnia & Herzegovina		Serbia	
	(1)	(2)	(1)	(2)	(1)	(2)
Male	0.037***	0.037***	0.034***	0.035***	0.013***	0.013***
	[5.52]	[5.62]	[5.68]	[5.97]	[2.66]	[2.68]
Age	0.006***	0.005***	0.006***	0.005***	0.0005	0.0003
	[3.00]	[2.98]	[3.32]	[3.22]	[0.29]	[0.18]
Age squared/1,000	-0.073***	-0.074***	-0.073***	-0.072***	-0.014	-0.012
	[3.12]	[3.18]	[3.28]	[3.39]	[0.65]	[0.56]
Married/Cohabiting	0.006	0.008	0.022**	0.021**	0.002	0.002
	[0.75]	[0.96]	[2.29]	[2.36]	[0.28]	[0.22]
Log(Number of Children)	0.007***	0.006***	-0.005	0.002	-0.004	-0.003
	[2.86]	[2.74]	[0.54]	[0.27]	[0.92]	[0.71]
Federation of Bosnia & Herzegovina	-	-	-0.009	-0.010	-	-
			[1.38]	[1.61]		
Urban region	0.020***	0.017**	0.008	0.005	0.010**	0.010*
	[2.69]	[2.34]	[1.32]	[0.87]	[1.96]	[1.85]
Low Education	-0.024***	-0.020**	-0.016**	-0.011*	-0.005	-0.003
	[3.10]	[2.54]	[2.51]	[1.79]	[0.83]	[0.55]
Disabled	-0.020**	-0.020**	-0.025***	-0.023***	0.011	0.008
	[2.43]	[2.32]	[3.23]	[2.95]	[0.80]	[0.65]
Another self-employed family member	0.143***	0.129***	0.087***	0.071***	0.012	0.01
	[3.65]	[3.43]	[3.77]	[3.45]	[0.87]	[0.78]
Log(Equivalized Household Consumption)	-	0.014**	-	0.030***	-	0.008
		[2.11]		[4.97]		[1.49]
Does not receive Remittances from abroad	0.003	0.005	0.017*	0.018**	0.003	0.004
	[0.19]	[0.36]	[1.96]	[2.37]	[0.25]	[0.41]
Remittances from abroad as a fraction of income	-0.0003	-0.0003	-0.002	0.003	-0.001	0.001
	[1.03]	[0.95]	[0.27]	[0.46]	[0.06]	[0.08]
Observed Probability	0.0474	0.0474	0.049	0.049	0.0249	0.0249
Predicted Probability	0.0306	0.03	0.0391	0.0367	0.0219	0.0216
Derivative Adjustment Factor	0.0297	0.0291	0.0376	0.0354	0.0214	0.0212
Number of Entries	156	156	222	222	88	88
Number of observations	3,293	3,293	4,531	4,531	3,531	3,531
Pseudo R^2	0.113	0.118	0.068	0.083	0.031	0.034
Log-Likelihood	-556.9	-554.1	-826.2	-812.2	-399.1	-397.9
Wald χ^2	111.7***	117.3***	111.0***	126.4***	30.4***	31.2***

Notes: Comments in Table 4 apply.

Table 8: Self-Employment Entry & Interaction Effects

Interaction with:		Log(Equiv. HH. Consumption)	Poverty	Formal Sector	Informal Sector	Unemployed/ Inactive	Agriculture	Employed Abroad
Formal Sector	Albania	-0.009 [0.62]	0.032 [1.49]	-	-	-	-	-
	BiH	**-0.031** [2.12]**	0.010 [0.82]	-	-	-	-	-
	Serbia	**-0.035** [2.22]**	**0.026* [1.95]**	-	-	-	-	-
Informal Sector	Albania	-0.010 [0.23]	0.014 [0.40]	-	-	-	-	-
	BiH	**0.033* [1.71]**	-0.003 [0.15]	-	-	-	-	-
	Serbia	**0.046* [1.78]**	-0.036 [1.40]	-	-	-	-	-
Unemployed/Inactive	Albania	0.001 [0.05]	-0.001 [0.02]	-	-	-	-	-
	BiH	0.012 [0.22]	**-0.025* [1.70]**	-	-	-	-	-
	Serbia	-0.005 [0.57]	-0.001 [0.01]	-	-	-	-	-
Agriculture	Albania	0.014 [0.60]	-0.031 [1.51]	-	-	-	-	-
	BiH	-0.015 [0.33]	0.075 [1.56]	-	-	-	-	-
	Serbia	0.009 [0.55]	-0.008 [0.70]	-	-	-	-	-
Employed Abroad	Albania	**-0.034* [1.88]**	**0.045* [1.84]**	-	-	-	-	-
	BiH	-	-	-	-	-	-	-
	Serbia	-	-	-	-	-	-	-
Informal Loan	Albania	-0.007 0.356	-0.024 [0.97]	0.001 [0.02]	0.031 [0.70]	0.018 [0.72]	-0.027 [1.07]	*No Entry (17)*
	BiH	-0.026 [1.51]	-0.005 [0.27]	-0.001 [0.07]	-0.006 [0.25]	0.014 [0.88]	**-0.068**[1.98]**	-
	Serbia	-0.005 [0.76]	*No Entry (55)*	**0.029* [1.86]**	*No Entry (13)*	*No Entry (44)*	*No Entry (38)*	-
Micro Loan	Albania	-0.006 [0.01]	-0.026 [0.78]	*No Entry (4)*	*No Entry (1)*	0.064 [0.33]	*No Entry (1)*	-0.055 [0.77]
	BiH	-0.019 [0.51]	0.031 [0.77]	*No Entry (38)*	**0.178** [1.96]**	*No Entry (51)*	*No Entry (8)*	-
	Serbia	-	-	-	-	-	-	-
Bank Loan	Albania	-0.021 [0.70]	*No Entry (7)*	0.071 [0.97]	0.154 [0.69]	*No Entry (11)*	*No Entry (6)*	*No Entry (2)*
	BiH	-0.016 [0.63]	0.016 [0.61]	**-0.052** [2.17]**	0.043 [0.86]	**0.041* [1.77]**	0.030 [0.39]	-
	Serbia	0.010 [0.41]	*No Entry (50)*	-0.013 [0.66]	0.008 [0.13]	0.014 [0.83]	*No Entry (14)*	-
Domestic Remittances	Albania	-0.012 [0.62]	-0.015 [0.62]	-0.001 [0.01]	0.005 [0.06]	0.023 [0.84]	-0.015 [0.61]	*No Entry (16)*
	BiH	-0.037 [1.48]	0.029 [1.23]	0.012 [0.59]	-0.032 [0.91]	0.002 [0.14]	0.054 [0.63]	-
	Serbia	0.024 [0.72]	*No Entry (95)*	-0.006 [0.31]	0.032 [0.57]	*No Entry (49)*	*No Entry (41)*	-
Remittances from Abroad	Albania	-0.007 [0.45]	-0.002 [0.12]	**-0.038* [1.93]**	**0.062* [1.76]**	-0.030 [1.60]	0.015 [0.73]	0.032 [1.10]
	BiH	-0.013 [0.92]	0.010 [0.59]	-0.013 [0.68]	-0.023 [0.88]	0.016 [0.96]	0.060 [0.84]	-
	Serbia	0.005 [0.25]	0.023 [0.72]	0.021 [0.76]	*No Entry (33)*	0.004 [0.19]	0.035 [1.12]	-
Institutional Remittances	Albania	0.004 [0.01]	0.001 [0.10]	0.020 [0.75]	-0.042 [1.03]	0.001 [0.06]	0.009 [0.36]	-
	BiH	-0.007 [0.04]	0.007 [0.09]	0.180 [1.55]	*No Entry (7)*	-0.062 [0.75]	*No Entry (3)*	*No Entry (6)*
	Serbia	0.051 [0.95]	0.003 [0.10]	0.034 [0.90]	*No Entry (26)*	*No Entry (30)*	0.056 [1.06]	-
Social Remittances	Albania	0.042 [1.41]	-0.027 [1.37]	**0.050* [1.91]**	**-0.056** [2.05]**	-0.006 [0.33]	0.015 [0.76]	*No Entry (44)*
	BiH	-0.002 [0.18]	0.004 [0.29]	-0.005 [0.35]	0.008 [0.27]	0.008 [0.55]	-0.025 [0.68]	-
	Serbia	0.025 [1.19]	-0.006 [0.43]	-0.003 [0.24]	-0.008 [0.26]	0.007 [0.50]	-0.007 [0.49]	-

Notes: * p<0.10, ** p<0.05, *** p<0.01. Marginal Effects [z-statistics]. The specifications are as in Column1 of Table 4, plus *Variable*, *Interaction Variable* and *Interaction Term*. The calculation of the interaction effects are based on Ai and Norton (2003), Norton and Ai (2004).

Table 9: Employment Generation

	Bosnia & Herzegovina			Serbia		
	Employer	*Own-Account*	*No Entry*	*Employer*	*Own-Account*	*No Entry*
Male	0.004	0.022***	-0.026***	0.003**	0.003	-0.006
	[1.45]	[5.01]	[5.07]	[1.99]	[0.91]	[1.62]
Age	0.001*	0.002*	-0.004**	0.0005	-0.001	0.0002
	[1.78]	[1.72]	[2.42]	[1.21]	[0.58]	[0.15]
Age squared/1,000	-0.021**	-0.029*	0.050***	-0.006	0.002	0.004
	[1.99]	[1.88]	[2.66]	[1.18]	[0.14]	[0.24]
Married/Cohabiting	0.009**	0.009	-0.018**	0.0004	0.006	-0.006
	[2.45]	[1.42]	[2.46]	[0.40]	[1.52]	[1.57]
Log(Number of Children)	-0.004	0.006	-0.003	-0.0001	0.001	-0.001
	[0.95]	[1.02]	[0.35]	[0.01]	[0.23]	[0.22]
Federation of Bosnia & Herzegovina	-0.006*	-0.0003	0.006	-	-	-
	[1.81]	[0.07]	[1.12]			
Urban region	-0.001	0.008*	-0.007	-0.0002	-0.004	0.004
	[0.22]	[1.74]	[1.36]	[0.18]	[1.08]	[1.06]
Low Education	-0.005	-0.009**	0.014**	-0.001	-0.001	0.001
	[1.57]	[2.00]	[2.53]	[0.44]	[0.11]	[0.23]
Disabled	-0.009***	-0.011**	0.019***	-0.0002	0.019	-0.019
	[2.67]	[1.99]	[3.05]	[1.47]	[1.52]	[1.52]
Another self-employed family member	0.011	0.056***	-0.067***	0.005	-0.003	-0.002
	[1.58]	[3.06]	[3.44]	[1.22]	[0.42]	[0.27]
Log(Equivalized Household Consumption)	0.014***	0.011***	-0.026***	0.002***	-0.001	-0.002
	[4.40]	[2.86]	[4.96]	[2.65]	[0.15]	[0.47]
Informal Sector	0.002	0.049***	-0.051***	0.021***	0.024**	-0.045***
	[0.57]	[4.23]	[4.16]	[2.68]	[2.47]	[3.69]
Unemployed/Inactive	-0.004	-0.002	0.006	0.0001	-0.002	0.002
	[1.11]	[0.33]	[0.90]	[0.40]	[0.41]	[0.41]
Agriculture	0.001	0.032*	-0.033*	0.007*	-0.012***	0.005
	[0.21]	[1.66]	[1.66]	[1.65]	[2.72]	[0.87]
Informal Loan	-0.009***	0.002	0.007	0.0002	-0.009**	0.009**
	[3.51]	[0.41]	[1.13]	[1.41]	[1.99]	[1.99]
Micro Loan	-0.004	-0.006	0.01			
	[0.73]	[0.72]	[0.99]			
Bank Loan	0.009*	-0.003	-0.002	-0.0001	-0.004	0.004
	[1.67]	[0.55]	[0.24]	[0.03]	[0.74]	[0.62]
Domestic Remittances	-0.003	-0.002	0.005	0.0003	-0.008*	0.007
	[0.57]	[0.37]	[0.64]	[0.17]	[1.67]	[1.54]
Remittances from Abroad	-0.011***	-0.005	0.016***	-0.002*	0.003	-0.001
	[4.51]	[0.97]	[2.72]	[1.76]	[0.27]	[0.12]
Institutional Remittances	0.049	0.064	-0.113**	0.001	-0.008	0.007
	[1.26]	[1.61]	[2.21]	[0.26]	[1.38]	[1.10]
Social Remittances	-0.003	-0.002	0.004	-0.001	0.005	-0.004
	[0.98]	[0.35]	[0.81]	[0.45]	[0.94]	[0.79]
No. of Observations	4,531			3,531		
Log Likelihood	-909.5			-405.5		
Wald χ^2	230.9***			160.4***		

Notes: * p<0.10, ** p<0.05, *** p<0.01. Multinomial Probit: Marginal effects and z-statistics. In the estimation, robust standard errors were implemented, clustered at the household level.

Table 10: Business Survival

	Albania			Bosnia and Herzegovina		
	Survivor	*Failed*	*No Entry*	*Survivor*	*Failed*	*No Entry*
Male	0.012***	0.005*	-0.017***	0.007***	0.009***	-0.016***
	[3.35]	[1.96]	[3.69]	[2.59]	[3.16]	[4.04]
Age	0.002*	0.001	-0.002*	0.003***	0.0004	-0.004***
	[1.87]	[0.72]	[1.88]	[3.67]	[0.55]	[3.03]
Age squared/1,000	-0.023*	-0.008	0.031*	-0.044***	-0.006	0.050***
	[1.90]	[0.78]	[1.95]	[3.79]	[0.54]	[3.17]
Married/Cohabiting	-0.001	0.006**	-0.005	0.006	0.004	-0.010*
	[0.19]	[2.31]	[0.91]	[1.63]	[1.04]	[1.81]
Log(Number of Children)	0.001	0.001	-0.001	0.001	-0.0004	-0.001
	[0.51]	[0.49]	[0.67]	[0.34]	[0.09]	[0.15]
Federation of Bosnia & Herzegovina	-	-	-	0.0001	-0.003	0.003
				[0.04]	[1.09]	[0.72]
Urban region	0.001	-0.001	-0.0001	0.005*	-0.0004	-0.005
	[0.24]	[0.30]	[0.03]	[1.72]	[0.16]	[1.10]
Low Education	-0.002	-0.013***	0.015***	-0.008***	-0.003	0.011***
	[0.53]	[2.91]	[2.66]	[2.67]	[1.07]	[2.62]
Disabled	-0.002	-0.0003	0.002	-0.008***	-0.008***	0.017***
	[0.38]	[0.11]	[0.36]	[2.91]	[2.65]	[3.87]
Another self-employed family member	0.029	0.02	-0.049**	0.028***	0.019*	-0.047***
	[1.57]	[1.31]	[2.03]	[2.73]	[1.65]	[3.07]
Log(Equivalized Household Consumption)	0.008**	-0.001	-0.008	0.012***	0.010***	-0.022***
	[2.16]	[0.21]	[1.61]	[4.06]	[3.43]	[5.19]
Informal Sector	0.033**	0.006	-0.040**	0.020***	0.008	-0.027**
	[2.28]	[1.12]	[2.51]	[2.74]	[1.12]	[2.31]
Unemployed/Inactive	0.003	-0.001	-0.002	0.004	-0.010***	0.006
	[0.58]	[0.42]	[0.33]	[1.17]	[2.63]	[1.13]
Agriculture	0.002	-0.003	0.001	0.002	0.015	-0.016
	[0.40]	[0.82]	[0.07]	[0.19]	[1.39]	[1.25]
Employed Abroad	-0.006	-0.005*	0.011*	-	-	-
	[1.01]	[1.89]	[1.66]			
Informal Loan	-0.010**	-0.007***	0.017***	-0.002	-0.004	0.005
	[2.05]	[2.68]	[2.71]	[0.52]	[1.25]	[1.22]
Micro Loan	0.18	0.127	-0.307	-0.002	-0.001	0.002
	[1.18]	[1.10]	[1.16]	[0.31]	[0.09]	[0.28]
Bank Loan	0.023	0.015	-0.038	0.006*	0.001	-0.007
	[0.87]	[0.87]	[0.88]	[1.77]	[0.31]	[1.24]
Domestic Remittances	0.002	0.03	-0.032	-0.008**	0.004	0.003
	[0.15]	[1.05]	[0.90]	[2.53]	[0.60]	[0.45]
Remittances from Abroad	-0.001	-0.0001	0.001	-0.006**	-0.010***	0.016***
	[0.13]	[0.02]	[0.11]	[2.12]	[3.63]	[3.98]
Institutional Remittances	-0.005	-0.004	0.009*	0.077*	0.015	-0.092*
	[1.10]	[1.42]	[1.68]	[1.69]	[0.58]	[1.81]
Social Remittances	0.002	0.004	-0.005	-0.005*	-0.0001	0.005
	[0.41]	[1.40]	[1.04]	[1.92]	[0.02]	[1.25]
No. of Observations		3,235			4,487	
	58	40	3,137	91	87	4,309
Observed Frequency	1.79%	1.24%	96.97%	2.03%	1.94%	96.03%
Predicted Probability	1.00%	0.60%	98.40%	0.96%	1.05%	97.98%
Log Likelihood	-436.4					-753.1
Wald χ^2	192.8***					221.3***