The impact of customs procedures on business performance: evidence from Kosovo

Mario Holzner and Florin Peci

Abstract

This paper aims to identify formal and informal institutional factors in customs procedures and their impact on the performance of small and medium-sized enterprises (SMEs) involved in international trade in Kosovo based on a questionnaire carried out in 2009. The econometric findings show that one of the most important obstacles encountered by SMEs are regular appeals against customs decisions, particularly those which reflect frequent changes in over-complicated laws and regulations. However, there is a positive and significant effect of the formal customs instruments that facilitate the trade in imported goods, namely 'customs procedures with economic impact'.

1. Introduction

The government institutions in transition countries are still regarded as ill-performing, fragile and weak in terms of the design and implementation of state policies. This has affected the economies of these countries, which suffer from a lack of general continuity in the economic sector; in particular, these obstacles are more pronounced for small and medium-sized enterprises (SMEs) (Hashi 2001). One of the biggest barriers for enterprises in transition countries is the low level of institutional development in relation to business regulation, as well as the business tax system (Aidis & Sauka 2005). The multitude of institutional policies affects the regular functioning of businesses and often plays a destructive role in the growth and performance of SMEs. Another example of the destructive role of state institutions in transition countries is the considerable number of unnecessary laws and regulations which regulate entrepreneurial activities and business operations. Such regulatory overload causes an increase in corruption and nepotism (Bartlett & Bukvič 2001; Smallbone & Welter 2001a; Djankov et al. 2002).

The role of SMEs in a country's economic, political, social and technical development continues to be the focus of an intensive debate between academics and policymakers. Generally, the scholars investigating SMEs consider these enterprises to be a key factor in economic growth, raising employment, supporting the formation of competitive markets, technical innovation and other aspects of socioeconomic development (Acs & Audretsch 1990; Storey 1994; Johnson & Loveman 1995). The importance of the role played by SMEs derives from the fact that the vast majority of enterprises are SMEs. Therefore, SMEs are considered to be generators of economic growth (Storey 1994; McMillan & Woodruff 2002; Audretsch 2007).

SME growth is also of great importance for countries in transition because of the radical changes that have occurred in command economies which discriminated against private companies whilst providing institutional and commercial support to public ones. The creation of a supportive environment which encourages the development of SMEs and bold entrepreneurship is one of the biggest challenges for transition countries.

Many authors have investigated the various obstacles faced by SMEs, including those that occur in transition economies (Bartlett & Prasnikar 1995; Blanchard 1997; Bartlett & Bukvič 2001; Hashi, 2001; Smallbone 2002; Pissarides, Singer & Svenjar 2003; Aidis 2005; Estrin, Meyer & Bytchkova

2005; Aidis & Estrin 2006). Their findings point to the fact that barriers caused by the existing business environment can usually be avoided and reflect an imperfect institutional framework. Such barriers include the uncertainty of duty and tax regulations, access to financial systems, as well as other obstacles which are particularly found in the early stages of transition (Schaffer & Weder 2001; Smallbone & Welter 2001b; Aidis 2005; Krasniqi 2007). The discussion on issues of entrepreneurship lies at the heart of the transition debate and focuses on the way entrepreneurship functions and the cost of obstacles which arise in this regard (Smallbone & Welter 2006).

The traditional role of customs as a state institution is characterised by responsibilities that include the collection of duties on internationally traded commodities, which is a common extension of the collection of other forms of taxes such as the Value Added Tax (VAT) and excise duties. However, the responsibility of the customs administration differs from one country to another. In developing countries, import duties are mainly collected as revenues for the national budget whereas in developed countries the main role of customs institutions is to protect the economy and enforce the law (Widdowson 2007). Certainly, customs procedures represent an important source of barriers to economic activity, especially for SMEs.

Hence, there are good reasons to analyse the impact of customs procedures on the business performance of SMEs in the case of Kosovo. This is a country where the private sector is dominated highly by SMEs, while the remaining socially-owned enterprises operate with minimum capacities at a time when they are awaiting the final phase of the privatisation process. SMEs make up 98% of all enterprises in Kosovo and represent a potential for significant economic growth (Riinvest Institute 2005). Given the small size of the country, involvement in international trade is of utmost importance even for very small companies. Also, the most recent historical developments make Kosovo an interesting subject to investigate.

Kosovo, as a country that is undergoing a process of transition, is characterised by various barriers inherited from the previous system and a high level of uncertainty in a marginalised context (Hoxha 2009). Kosovo is a developing country which is entering a new phase in its history as one of the world's most recent independent states.[1] However, even before the war in 1999, the economy of Kosovo faced many problems in relation to its political and institutional setup and this remains the case today. Problems include a privatisation process that is accompanied by high unemployment, excessive import growth, weak export sector, growing budget deficits and an informal economy (Riinvest Institute 2005). Thus, Kosovo – as one of the last Southeast European (SEE) countries to undergo the process of transition – provides a unique case study for investigating formal and informal barriers that have an impact on the growth and development of entrepreneurship.

Kosovo is also interesting due to the fact that several international and supranational organisations helped establish state institutions, including the customs administration. Kosovo Customs was established in August 1999 by the pillar of the European Union (EU) that was working under the auspices of the United Nations Mission in Kosovo (UNMIK). The UNMIK Customs Service was responsible for ensuring the application of fair and uniform trade regulations and other provisions applicable to goods subject to customs procedures. In December 2008, UNMIK transferred its competencies entirely to the Kosovan institutions. The activities and functions of Kosovo Customs are regulated by the new Customs Code of Kosovo which was adopted by the Assembly of Kosovo on 11 November 2008.

Considering the issues mentioned above, this study contributes to the available literature by analysing how customs procedures affect SMEs' growth and performance. In many respects, Kosovo represents an extreme case. It is a tiny country which has a small-scale business community dependent on foreign trade, is exposed to highly frequent institutional change and exists within a unique post-war environment characterised by a transitional economy. Kosovo is therefore a case study of general interest which could provide insights into the role of compliance costs.

The remainder of the paper is organised as follows. In section 2 we develop the research questions and a set of hypotheses tested in this paper. Section 3 describes the data and research methodology employed. The results of the investigation are discussed in section 4 and the final section presents the conclusions.

2. Research questions and hypotheses

On the basis of the discussion above, we can formulate the following research questions: what are the main factors affecting the turnover growth of SMEs engaged in international trade? Are there differences regarding the effects of these factors on the level of turnover achieved by SMEs engaged in international trade? What are the main formal and informal barriers to the activities of firms involved in international trade? Are customs institutions really making efforts to facilitate trade? Based on these questions we can develop a number of hypotheses.

We start from the assumption that an increase in the educational level of human capital in a firm will have a positive effect on its growth. This is supported by a number of authors who have analysed other aspects contributing towards the growth of firms. Becker (1964) focuses on differences between formal education and the acquisition of skills and knowledge that has a narrower scope of application, thereby defining general and specific human capital. Highly educated entrepreneurs play an important role in identifying and exploiting opportunities (Ucbasaran, Westhead & Wright 2006). According to Chandler and Hanks (1998), increased levels of human capital can act as a substitute for financial capital. Highly educated entrepreneurs are particularly successful when they own the firm in question; their educational level enables them to identify and select firms which have high growth expectations (Wasilczuk 2000; Almus 2002). Thus, we propose the following hypothesis:

H_1: *SMEs engaged in international trade that are managed by well-educated managers have higher turnover growth.*

Individuals with higher levels of specific human capital are better suited to understanding neglected business opportunities and making effective strategic decisions (Colombo & Grilli 2005). These agents have what is usually referred to as 'know-how', and 'tacit abilities' that are often decisive for a successful enterprise (Jovanovic 1982; Westhead & Storey 1996). Specific knowledge on customs transactions is also an aspect of specific human capital. If it is not present in the enterprise, external consultants can be hired. Thus, we formulate the following hypothesis:

H_2: *SMEs engaged in international trade that hire consultants for customs transactions will achieve higher turnover growth.*

Based on Gibrat's Law (1931), firm growth is independent of the size and age of the firm. Jovanovic (1982) has opposed this view, claiming that new firms learn from previous periods and experience which enables them to grow faster and survive. Other rejections of Gibrat's Law can be found in Geroski (1995), Suton (1997), Caves (1998) and Almus (2002). The results of the research regarding the validity of Gibrat's Law largely depend on the methodology applied. Using a standard regression model and kernel regression estimators in a sample of 2,188 Spanish firms, Farinas and Moreno (2000) conclude that both failure rates and the mean growth rate of successful firms decline with the size and age of firms. It should be stressed that their analysis was built on Jovanovic's (1982) theoretical growth model for firms called 'the noisy selection model', which is based on the lifecycle learning theory approach. The validity of Gibrat's Law for newly established firms was tested also by Lotti, Santarelli and Vivarelli (2003) in a sample of 1,570 such firms in the Italian manufacturing sector. While Gibrat's Law applies after the new firms have achieved the size necessary to overcome the minimum efficient scale, it does not hold true for firms in five out of six industries analysed in the years immediately following their start-up. In the case of Kosovo, the validity of Gibrat's Law was investigated by Krasniqi (2006), who concluded that the Law does not hold true for the firms he analysed in the SME sector. These included firms involved in trade, production and services. Accordingly, we can make the following two hypotheses regarding the size and age of firms:

H_3: *SMEs engaged in international trade that have a higher number of employees have lower rates of growth of turnover.*

H_4: SMEs engaged in international trade that exist for a longer period of time have lower rates of growth of turnover.

The frequency of the exchange of information with customs authorities and the way in which this information is gathered and exchanged can be seen as factors in improving a firm's efficiency because of their potential to reduce transaction costs (Verwaal & Donkers 2003). In general, the procedures applied in exchanging this information include the filing of a declaration for each import or export transaction. Simplifying this procedure by combining various transaction data into a single administrative customs declaration (SAD) will reduce the filing frequency and thereby the transaction costs. It is also possible to reduce the frequency of filing if firms that have met certain conditions are allowed to declare imports on a monthly basis. In turn, these simplified procedures enable firms to spend less time on gathering data and preparing customs documentation. We therefore state the following hypothesis:

H_5: SMEs engaged in international trade using simplified customs procedures will face a decrease in transaction costs and experience higher turnover growth.

Firms involved in international trade can also use other beneficial customs procedures, namely 'procedures with economic impact'. These offer, for example, exemption from the obligation to pay customs duties on imports provided the goods are not released into free circulation. These procedures form part of the trade facilitation measures introduced by the World Trade Organization (WTO) and the World Customs Organization (WCO) as a result of the pressure brought by businesses to abolish trade barriers in the interests of economic development. The firms authorised by customs authorities to use these procedures will obtain the same benefits as in hypothesis H_5, (that is, a reduction in compliance costs). These considerations result in the following hypothesis:

H_6: SMEs engaged in international trade that use procedures with economic impact have higher turnover growth.

In transition countries, many formal barriers are caused by the general regulatory environment, high levels of taxation, skills requirements, complicated laws and regulations that are amended frequently as well as a low level of law enforcement (Bohata & Mladek 1999; Glas, Drnovsek & Mirtic 2000; Barlett & Bukvič 2001; Hashi 2001; Ačevska, Bartlett & Stojanova 2002; Pissarides, Singer & Svenjar 2003; Aidis 2005; Xheneti 2006; Krasniqi 2007). The early years of transition are characterised by state employees' lack of experience and knowledge of the market economy which results in their inability to provide appropriate services to businesses. This results in procedures which are costly and time-consuming, an inadequate legal system and deficiencies typical of the process of transformation which are serious obstacles for business growth (Krasniqi 2007). Thus, we can develop the following hypothesis:

H_7: SMEs engaged in international trade that put forward regular complaints and appeals against the customs decisions have less turnover growth.

The growth of firms is not only hindered by formal barriers to trade. Informal barriers, particularly those relating to corruption and the unofficial economy are also problematic. We will refer to them as barriers confronted by the firms as a consequence of the low ethics of officials. In both developed and developing economies, a heavy-handed bureaucracy is considered a risk for business growth. This includes an inappropriate tax system and various discriminatory legal regulations – particularly complicated laws, rules and regulations – that regulate the functioning of companies (Bartlett & Bukvič 2001). It is important to note that the over-regulation of companies often leads to regulatory evasion by entrepreneurs. This, in turn, increases the grey economy and encourages the devotion of resources to influence the regulatory environment in their favour, thereby encouraging 'unproductive entrepreneurship' (Baumol 1990).

Surprisingly, Xheneti (2006) has found evidence that corruption-related barriers positively affect firms' growth: he argues that corruption seems to be a way to cope with transitional problems and 'buy' a rapid pace of institutional change. He concludes that corruption can be an informal institutional mechanism

(that is, 'grease for the wheels' of growth), which is apparently effective in overcoming many of the frictions which would otherwise inhibit business growth.

The report of the World Bank (2005) shows that corruption has been mentioned as a severe obstacle to investment by 20% of respondents in emerging markets, as well as a major obstacle by 15% of respondents in a survey of more than 26,000 firms in 53 countries (World Bank 2005). The interdependence of formal and informal barriers and their interrelationship have been analysed by Smallbone et al. (2001) for Belarus and Aidis (2005) for Lithuania. It is important to note that in his study, Aidis identifies the implementation of business regulations, the high frequency of tax inspections, the long time spent on negotiations and the corruption of tax inspectors as the most frequent informal barriers. In Kosovo's context, Krasniqi (2007) surveyed 600 SMEs during 2002, concluding that the growth of Kosovo's SMEs is impeded by several informal barriers, unfair competition and corruption. Consequently, corruption harms the development of the SME sector for the simple reason that it increases the transaction costs of businesses. Based on what has been said above, we can make the following two hypotheses:

H_8: *SMEs engaged in international trade that are confronted by low ethical standards among customs officials have lower turnover growth.*

H_9: *SMEs engaged in international trade that are subject to frequent customs audit controls have lower turnover growth.*

The density of imports to be cleared at certain entry points ('clearance density') is yet another important variable that influences business efficiency, by increasing or decreasing the transaction costs of imports. In Kosovo, the highest clearance density – and consequently, the most time spent on clearance – is at the Hani i Elezit entry point, which is the busiest border crossing for imports in the Balkans. The clearance times here are considerably longer than at other entry points. Therefore, firms importing their goods via this border crossing face higher transaction costs due to the longer time needed for clearance. Accordingly, we formulate our final hypothesis as follows:

H_{10}: *SMEs engaged in international trade that declare goods at the entry point with the highest density of clearance will have higher transaction costs and thus a lower rate of turnover growth.*

3. Data and methodological approach

In this section, we present empirical evidence for the impact of transaction costs and other impediments on the business performance of 122 SMEs that operate in the trade and manufacturing sectors in Kosovo. The sample was randomly selected from the business register in the database of the Ministry of Trade in Kosovo, where more than 4,000 operational firms are involved in international trade.[2] This figure represents more than 3% of the total population of Kosovan SMEs engaged in international trade. The sample covers businesses across all regions of Kosovo and reflects their size, including micro enterprises, small enterprises and medium-sized enterprises. Out of 160 contacts, 122 agreed to be interviewed, resulting in a response rate of over 76%.

According to the European Commission's[3] definition of SMEs (which is based on the number of employees), the sample contains 42 micro enterprises (less than nine employees), 77 small enterprises (between 10 and 49 employees) and three medium-sized enterprises (between 50 and 249 employees). The firms represented have an average age of 7.5 years in the year of the survey (2009) and an average of 13 employees. As far as the legal form is concerned, the sample contains three public limited companies, 10 limited liability companies and 109 private companies.

Approximately 73% of the firms included in our sample belong to the trade sector, another 10% are involved in manufacturing production and the rest are active in other services sectors. Around 10% of the firms in our sample have an annual turnover of more than one million euros.

The questionnaire was developed in accordance with various stakeholders involved in international trade in Kosovo: the business committee, chamber of trade and industry, trade alliances, border agencies, and others. The questionnaire was completed between February and March 2009, with the resulting data processed in April 2009. From this, we created and developed a database with several indicators. The questionnaire covers general information about the firm's turnover, number of employees, company age, etc. The interviews were conducted face-to-face with the key people responsible for the activities of each enterprise (that is, mainly owners or general managers). The survey also contains information concerning the perception of entrepreneurs regarding the business environment and customs procedures.

One of the main issues in firm growth studies is the lack of longitudinal research (Davidsson 2005) – growth being a phenomenon that necessarily happens over time. In this study, however, the time dynamic that would illustrate the effects of the institutional environment is limited to only one period of SMEs' growth between 2008 and 2007. This is because our database does not contain longitudinal data. Only the data on turnover and employment exist separately for the years 2007 and 2008 respectively. Considering this, future research should try to include panel data techniques when studying the growth of firms, particularly within the context of transition where the formal and informal institutional environment changes constantly and thus affects SMEs' growth. Future research into the growth of Kosovan firms should also take into account growth indicators other than turnover growth (for example, sales, profits and employment growth), compare results and observe any changes which occur when a particular growth indicator is introduced.

The analysis is based on a cross-sectional database for the year 2008 with limited information for 2007. The dependent variable is the rate of turnover growth experienced by a firm in 2008 that trades on the international market (GRO). A firm is considered to be an '*exporter-importer*' if it is more than three years old and has submitted more than 20 customs declarations on a cross-border entry point (that is, a Terminal Clearance Station of Kosovo).

The independent variables are mostly qualitative in nature whereas variables such as the number of employees, consultancy costs and firm age are measured quantitatively. The remaining variables such as the education of managers, Hani border crossing location, use of simplified procedures, ethics of customs officials, appeals, audit control, and procedures with economic impact are converted into dummy variables of one if the respective barrier to firm turnover growth is recorded and zero otherwise.

1. Education of managers (EDU): This human capital variable is expected to positively correlate to the firms' turnover growth. The variable is one if the respondent has a university education and zero otherwise.

2. Consultant costs (CON): It is expected that firms which hire costly but knowledgeable and helpful experts for the trade and customs transactions will have higher turnover growth. Consultant costs are measured in euros.

3. Employees (EMP): We take the number of employees in the year 2007. It is expected that this variable will have a negative influence on turnover growth.

4. Age of firms (AGE): It is expected that this variable will have a negative influence on turnover growth. It measures the number of years that the firm is active.

5. Use of simplified procedures (SIM): Under this procedure, imported goods will have a higher turnover and transaction costs should be reduced. The variable will be one if firms use simplified procedures and zero otherwise.

6. Use of procedure with economic impact (ECO): Traders who use procedures with economic impact are expected to have higher rates of turnover growth. Thus, for firms that use procedures with economic impact the variable will be one and zero otherwise.

7. Appeals (APP): Appeals are time-consuming and costly. Therefore, they will cause an increase in transaction costs. The variable is one if the trader has appealed and zero otherwise.

8. Customs officials' ethics (CUS): This variable represents the 'bad behaviour' of customs officials such as red tape and corruption. Where such behaviour occurs, the variable is one and zero otherwise. This represents a qualitative variable and we evaluate answers rating one on the scale ('very bad') with one, and those from 2 to 5 with zero.

9. Audit control (AUD): This is also time-consuming and increases compliance costs for the firms. The variable is one if the firm has undergone an audit and zero otherwise.

10. Hani location of clearance (HAN): It is expected that this variable will have a negative influence on turnover growth because 40% of all customs clearance is concentrated at the Hani location, which involves congestion costs.

The empirical model is defined as follows and will be estimated using a stepwise ordinary least squares (OLS) estimator:

$$GRO_i = \alpha_0 + \alpha_1\ EDU_i + \alpha_2\ CON_i + \alpha_3\ EMP_i + \alpha_4\ AGE_i + \alpha_5\ SIM_i + \alpha_6\ ECO_i + \alpha_7\ APP_i + \alpha_8\ CUS_i + \alpha_9\ AUD_i + \alpha_{10}\ HAN_i + \varepsilon_i.$$

In addition, we include a dummy variable for the few exporting firms[4] in the sample to see whether it improves performance. We perform a stepwise estimation procedure, starting with the full model and progressively removing the least significant variable. Thus, we will only present the results for an empirical model whose co-efficients have a significance of at least 10%. A Breusch-Pagan/Cook-Weisberg test for heteroskedasticity in our data rejects the zero hypothesis of constant variance and thus all calculations are performed in a robust way. None of the variables correlates with each other to a great extent and we can therefore rule out any multi-collinearity (see correlation matrix in the appendix). As a robustness check we also calculate different sub-samples such as one without exporting firms and one without firms having negative turnover growth. Moreover, in an alternative calculation we use the 2008 turnover level in euros as the dependent variable with additional explanatory variables such as the turnover in 2007 as well as the squared terms of the number of employees and consulting costs in order to check for possible endogeneity and non-linearity for some of the variables.

4. Empirical findings

Using the equation above, our calculations provide the following results. Hypotheses 1 and 2 regarding the higher education of managers and involvement of consultants for customs transactions are valid. Both coefficients are positive and significant and can be interpreted as follows. An increase in consulting costs of 1,000 euros increases a firm's turnover growth by 1.4%. If a firm's manager has tertiary education, the turnover growth was found to be higher by almost 13%. Our calculations also support hypotheses 3 and 4. We find a negative correlation between the number of employees and number of years that the firm has been active in terms of turnover growth, with both coefficients being highly significant. These results do not support Gibrat's Law but are in line with the findings of other studies (see Krasniqi 2006, 2007). From the set of customs-related indicators, only two were significant. These are the use of procedures with economic impact as well as the appeals variable. While the former coefficient is highly significant, the latter is only significant at the 10% level. The coefficient for the use of procedures with economic impact is positive and the coefficient for the appeals variable negative. The coefficients of both dummy variables are similar in size, indicating that the use of the former relates to higher turnover growth of approximately 12%, whereas turnover growth is 11% less for firms involved in appeals. All other customs-related coefficients are insignificant, indicating that the use of simplified procedures, perceived bad customs behaviour, audits and congested customs clearance locations are not significantly related to the turnover growth of Kosovan SMEs. The exporter dummy variable proved to be insignificant. The

R² of the model is at about 28%. Thus, there are obviously other important determinants of turnover growth which are missing in our database. Using hierarchical procedures to calculate delta R²s allows us to estimate how the individual explanatory variables add to the explained variance of the model. Of the overall 28% of the model's R² about one quarter is related to the variable years of a firm's activity, while approximately one-fifth of the model fit is attributed to the education of managers and procedures with economic impact. Each of the other three significant variables covers about one-tenth of the model's explanatory power.

Table 1: Determinants of Kosovo SMEs' turnover growth, 2008

	Coefficients	**P-value**
Constant	35.752	0.000
Education of managers	12.950	0.003
Consulting costs	0.001	0.017
Number of employees 2007	-0.459	0.002
Years of firm's activity	-2.381	0.000
Procedure with economic impact	11.698	0.006
Appeals against customs decisions	-11.280	0.082

N = 122

R² = 27.7%

Estimator: Stepwise OLS, robust standard errors.

The robustness check using different sub-samples (such as one without exporting firms and one without both exporting firms as well as firms having negative turnover growth) yielded the following results: in both cases the appeals coefficient turned insignificant; all other results remained stable compared to our main calculation. This draws attention to the fact that exporters and firms with negative growth were more likely to be involved in troublesome customs appeals.

We also conducted an alternative calculation explaining the level of 2008 turnover in euros as the dependent variable with additional explanatory variables such as turnover in 2007 as well as the squared terms of the number of employees and consulting costs in order to check for possible endogeneity and non-linearities. One abnormal observation had to be removed from the data set. Interestingly, the results do not differ greatly from the growth model. Almost the same variables have coefficients of the same sign (that is, positive/negative) and significance. Again, the managers' education as well as the consultancy costs prove to be positively correlated with the dependent variable. Only now, the squared consulting costs have a negative coefficient. This implies that expenditure on consultancy in customs issues exhibits a diminishing return. Instead of the number of employees, the squared number of employees is significant in explaining less turnover. This indicates that, in terms of employees, only larger firms are at a disadvantage. The number of 'firm years' again has a negative coefficient. There are no changes concerning the customs-related coefficients either. The coefficient for the use of procedures with economic impact is positive and the coefficient for the appeals variable negative. In this model, the R² is more than 99%. This is certainly due to the inclusion of the lagged turnover variable.

Table 2: Determinants of Kosovo SMEs' turnover level, 2008

	Coefficients	**P-value**
Constant	20862.060	0.172
Turnover level 2007	1.104	0.000
Education of managers	20531.520	0.015
Consultancy costs	10.271	0.000
Consultancy costs squared	-0.001	0.029
Number of employees 2007 squared	-42.722	0.036
Years of firm's activity	-3492.184	0.004
Procedure with economic impact	26436.700	0.001
Appeals against customs decisions	-15595.480	0.097

N = 121

R^2 = 99.4%

Estimator: Stepwise OLS, robust standard errors

5. Conclusions and policy implications

Our research suggests that regular appeals against customs decisions represent one of the most important institutional obstacles encountered by SMEs in the import-export sector. This supports earlier results on Kosovo by Krasniqi (2007). However, there is also a positive and significant correlation of formal customs institutions that facilitate the trade of imported goods, namely 'procedures with economic impact'. This result supports the efforts made by the WTO and WCO in the field of trade facilitation. In this respect, another determinant that is positively related to turnover growth is the engagement of experts in the field of customs clearance procedures. However, the level of turnover will suffer if the expenditure for consultancy is too high. This suggests that institutional support should be directed towards the simplification of customs procedures in order to reduce the compliance costs of firms. Also, law enforcement needs to be put in place more effectively.

The fact that a large number of employees and many years of business activity negatively influence both growth and the level of turnover send a reassuring signal to new entrants in this market. Also, this reaffirms earlier results by Krasniqi (2006, 2007) and complements literature that empirically rejects Gibrat's Law (1931). However, it was also found that it is beneficial for a firm to have a well-educated management team. This should be an additional incentive for the public and private sectors to invest in the education of Kosovo's population. Although not very surprising, this result confirms the earlier findings of Wasilczuk (2000) and Almus (2002).

It is interesting to note that, contrary to popular belief, customs behaviour perceived as 'bad' such as red tape and corruption as well as audit controls, apparently do not influence the level and growth of turnover of Kosovan SMEs engaged in international trade. Here, our findings do not match earlier results on Albania and Kosovo. In the former case, Xheneti (2006) found a positive relationship and in the latter case, Krasniqi (2007) observed a negative correlation. Thus, it seems that reforms of formal customs procedures are most likely to improve the efficiency of doing business in Kosovo. However, simplified procedures aimed at reducing the time spent filling out declarations have not proved significant. This contrasts to what Verwaal and Donkers (2003) found in their Dutch sample.

Thus, while it has to be noted that the policy recommendations offered do not necessarily follow directly from our empirical research, the assumption is that some of the main barriers to doing business in the import-export sector in Kosovo are a consequence of frequent changes in over-complicated laws and regulations. The link between state laws, regulations and policies and the parameters important for economic well-being of SMEs in Kosovo is a subject which deserves more detailed analysis in future research.

Appendix

Appendix Table 1: Correlation between coefficients at a 10% level of significance

	growth	turnov.	educat.	consult.	empl.	years	simple	econ	appeals	behav.	audit	hani
growth	1											
turnov.	-0.197	1										
educat.	0.229		1									
consult.	0.165	0.224		1								
empl.	-0.166	0.503		0.268	1							
years	-0.293					1						
simple							1					
econ	0.223	-0.207	-0.287					1				
appeals	-0.211								1			
behav.				-0.210						1		
audit									0.205		1	
hani										0.165		1

Appendix Table 2: Descriptive statistics

Variables	Mean	Std. Dev.	Minimum	Maximum
Turnover growth 2008	19.9	23.9	-88.8	131.6
Turnover level 2008	418942	507901	28000	3135000
Education of managers	0.344	0.477	0	1
Consulting costs	2207	3201	0	13800
Number of employees 2007	11.8	8.2	2	55
Years of firm activity	5.7	2.3	3	23
Simplified procedure	0.238	0.427	0	1
Procedure with economic impact	0.434	0.498	0	1
Appeals against customs decisions	0.836	0.372	0	1
Bad customs behaviour	0.500	0.502	0	1
Audit	0.861	0.348	0	1
Hani	0.459	0.500	0	1

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Notes

1   From June 1999 the territory of Kosovo was administered by the United Nations Mission in Kosovo (UNMIK). On 17 February 2008, in an extraordinary session the parliament of Kosovo unilaterally declared Kosovo's independence and with the promulgation of the constitution of Kosovo, the institutions of the Republic of Kosovo took over all governance authorities.

2   We did not include firms that were inactive in the period 2005 to 2008.

3   http://europa.eu.int/comm/enterprise/enterprise_policy/sme_definition/index_en.htm.

4   The vast majority of Kosovo firms engaged in international trade are solely importing. The country has not yet developed a proper export sector.

Mario Holzner

Mario Holzner is staff economist at the Vienna Institute for International Economic Studies. His research focuses on international trade, economic growth, income distribution, and the economies of Southeast Europe. Mario completed a doctorate at the Vienna University of Economics and Business administration (economics). In his recent research, Mario analysed the effects of free trade agreements for Balkan economies with the help of the Global Simulation Model (GSIM).

Florin Peci

Florin Peci has worked for 11 years on organisational development and management reform in Kosovo Customs. He provided advice on issues concerning customs performance on several United Nations and European Community-funded technical assistance projects in Kosovo, and on issues concerning customs competencies, customs legislation, performance measurement in Customs, and questions concerning the design of customs management information systems. Currently, Florin is Head of the Law Enforcement Department in Kosovo Customs and is a PhD candidate at the Economic Faculty, University of Prishtina in Kosovo.