

# Is Doing Business Report a Good Tool for Describing Business Regulation in All Countries? (A Serbian Perspective)



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**M**arket regulation has long been one of the significant topics in social sciences since at least the 19<sup>th</sup> century, with two main opposing views coming from different schools of thought. First, that regulation is necessary to reach desired social goals and increase economic efficiency; and second, that regulation is unnecessary since it leads to economic waste and erodes individual choice and freedom. However, since there were no reliable instruments of measuring the overall quality of the regulatory environment in different countries and over time, there was a clear need for a tool which would measure just that. This gap was successfully bridged with the introduction of the *Doing Business* (DB) report by the World Bank in 2003, which covered a large number of countries and areas important for small and medium enterprises. This sparked a new wave of interest in empirical research regarding the effects of business regulation.

Throughout the years, the DB has become one of the key international benchmarks. Its publication is awaited by the media and policy makers across the world to help evaluate reforms various governments have implemented. Its rankings and data are widely used for investment and business decisions by private company's management and for making other international benchmarks (such as *Index of Economic Freedom* by Heritage Foundation). Due to its prominence, many governments across the world have been willing to make long strides in order to improve its rankings in the DB, in order to attract foreign investors, improve its image in the business community and increase its economic growth. Empirical research supported these efforts, since it implied that a better score in the DB really leads to higher economic growth.

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This was also the situation for countries in transition. Since their background was even more difficult for conducting business than those of over-regulated advanced market economies, due to their authoritarian background, lower quality of administration, weak rule of law, rampant corruption, and other legacies of the centrally planned economy and state socialism, many transition econo-

mies made more efforts in advancing their DB rankings over the years. This has led to somewhat paradoxical situations: is it really so, that regulatory environment is more business friendly in Georgia (ranked 6<sup>th</sup> in the DB) than in the United States (8<sup>th</sup>), or the United Kingdom (9<sup>th</sup>)? Or that business in Macedonia (10<sup>th</sup>) is less burdened than in Sweden (12<sup>th</sup>) or Australia (18<sup>th</sup>)? Or that Belarus (37<sup>th</sup>) is a better business destination than Switzerland (38<sup>th</sup>)? Truth be told, the *Doing Business* report has lost a significant part of its explanatory power, at least for countries in transition, due to political economy of reforms and disregard of the level of rule of law.

### METHODOLOGICAL INTRODUCTION

The methodology of the *Doing Business* report slowly evolved over the time. It now includes the following areas:

- starting a business;
- dealing with construction permits;
- getting electricity;
- registering property;
- enforcing contracts;
- getting credit;
- protecting minority investors;
- paying taxes;
- trading across borders;
- resolving insolvency.

These business regulation areas measure the administrative burden associated with an area of doing business, such as the number of administrative tasks, the time necessary for them, and associated monetary costs. Data on actual performance are gathered and transformed to a 0–100 scale, where the maximum number of points is allotted to the best performer. Further important information is also gathered, but not included in the scores, such as labor market regulation and contracting the government (tackling the procurement process).



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*Doing Business* of the World Bank clearly states in its methodological section that there exist several misconceptions about it. This being said, there are other notable problems with this survey, which makes its results dubious – especially for transition countries. These are as follows:

- 1) DB is not a comprehensive measure of a business environment;
- 2) focusing on increasing the DB ranking is a relatively easy task;
- 3) DB envisages that all regulation is fully and impartially implemented;
- 4) focusing on the major city only may give biased results.

Furthermore, the DB also implies that legal stipulations are fully and impartially implemented in areas where legal documents are used as a data source, which can be a far cry from the actual situation in countries historically plagued with weak institutions. There is also the problem of using the nation's capital

as a proxy for regulatory environment. Due to all these constraints, which will be further elaborated on, the widespread use of the *Doing Business* scores and rankings should be used with great caution, since it presents the regulatory environment in countries in transition in a more positive light than actually is the case.

### **NARROW FOCUS OF DOING BUSINESS: TREES IN A FOREST**

Measuring the character of business regulation is not an easy task. When international benchmarks that try to evaluate the character of business regulation in a country are taken into account (such as *Economic Freedom of the World* by the Fraser Institute, *Index of Economic Freedom* by the Heritage Foundation, *Doing Business* by the World Bank or *Global Competitiveness Report* by World Economic Forum), it becomes clear that they use either hard data (such as a duration or costs of a procedure, level of tax rates etc.), perception of business people and experts, or a mix of both. Objective data are more reliable, but they are narrower since they can be used to depict a situation in several areas only; on the other hand, perception of business people regarding business regulation they face in their everyday activities is more general in scope, but also almost impossible to describe the situation in detail. The former approach cannot see the forest since it focuses on individual trees, while the latter cannot see individual trees from the forest.

The DB uses exclusively objective parameters. This means that it had to restrict its coverage of regulatory environment, in order not to lose itself in too many details that may not be too relevant for the overall character of the regulatory framework at hand. This narrow view, however, leaves out a lot of regulatory areas which may also be important since the regulatory framework



THE WIDESPREAD USE OF THE DOING BUSINESS SCORES AND RANKINGS SHOULD BE USED WITH GREAT CAUTION, SINCE IT PRESENTS THE REGULATORY ENVIRONMENT IN COUNTRIES IN TRANSITION IN A MORE POSITIVE LIGHT THAN ACTUALLY IS THE CASE

in modern countries is measured in tens of thousands of pages. For example, the *acquis communautaire* or the common EU legislation is considered to be nearing 170,000 pages, while the recent total survey of business regulation in Serbia has recently been estimated to be more than 80,000 pages [See Table 1].

At the same time, the regulation assessed by the DB is several thousand pages in length at the most. For example, the "Paying Taxes"

Table 1: Scope of business regulation in Serbia

Area	No. of regulations	No. of pages
Government system	41	327
Defense, military, and internal affairs	250	2 891
Judiciary, penal legislation, and litigation	57	1 034
Public revenues	338	3 940
Monetary system, financial organizations, and financial business	247	5 135
Property and obligations, family and marital relations	241	3 684
Labor relations and employment	187	2 765
Development	557	5 800
General economy regulations	358	3 719
Goods of general interest and environment	711	8 361
Retail, tourism, and hospitality	112	1 685
Construction, land, and communal utilities	255	13 602
Agriculture	470	5 840
Transportation, networks and energy	635	10 726
Public institutions, science, education, culture and media	368	3 467
Social insurance, healthcare, social care	420	8 882
Total	5 247	81 858

Source: National legal database. Available [online]: <https://www.pravno-informacioni-sistem.rs/SIGlasnikPortal/reg/content>

segment covers only the total number of payments per year, the number of hours necessary to administer them, total taxes and contributions as a % of profit, and post filing index covering tax audits and refunds. These well may be the most important parts of tax regulations, but this hardly covers the almost 4,000 pages length of tax regulations in Serbia.

Therefore, since the DB is rather narrow, it means that regulation outside of its scope can still be very burdensome, but this will not have an impact on a country's rank in the report.

**INCREASES IN DB SCORE:  
IF MEASURED – REFORM IT,  
IF NOT – LET IT BE**

Since the DB is both narrow and transparent, and relies on objective data only, it is easier to implement regulatory reforms that would boost a country's score and improve its ranking, compared to other international indices that also measure business regulation. Furthermore, the DB does not have an ideological flair that some other benchmarks do, so it is politically more appealing to use it as a policy measure. But this also means that there is a danger of over focusing only on the DB indicators, at the detriment of other important measures of regulatory quality. A clear example of this could be found in the names of several government working groups that are active in the field of regulation improvements: instead of being called *working groups for improvement of business regulation*, they are often named *working groups for improvement of DB ranking*, as was the case in Serbia.

Local reform initiatives in the field of reforming business regulation can also support partial moves that would increase a DB score. The most important reasons for this are DB transparency: it is easy to identify areas in which reforms are necessary, and

people responsible. For example, in the area of building licenses, the minister for infrastructure, head of the cadaster office etc., so it is possible to incentivize politicians and civil servants to take over the responsibility for it, since they could be easily blamed for failures but could also reap accolades if successful – which is almost impossible in the case of other, more general benchmarks.

The role of international financial institutions, most notably the International Monetary Fund (IMF), can also have an impact on preferring the DB over other benchmarks. In case of an IMF-backed program, the local IMF office also usually supports measures that would improve the local business climate, which would be attested by improvement in international indices. However, these programs are usually not long (up to three years) so results need to be reached relatively quickly, and they include a quar-

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terly screening in order to evaluate improvements. For these kinds of programs, the DB is the ideal benchmark: it is easy to create lists of measures that need to be taken, and it is possible to follow if and when they are actually implemented. It is also possible to make a model that would predict improvement in score and rank that would be brought by an individual reform.

These DB characteristics could explain why some countries have had a significant improvement in their DB score or rankings, but not so stellar results in other regulatory benchmarks. One of these countries is also Serbia, which has, in recent years, significantly improved its DB position.

Since 2014, the country has substantially increased its DB rank, but at the same time its score in the “Burden of Government Regulation” from the *Global Competitiveness Report* (GCR) has increased only slightly [See Table 2]. Furthermore, the data from the US Aid Business Enabling Project, which quantified administrative burden in the percentage of GDP on the economy by using the Standard Cost Model (SCM), showed that there was also only an incremental decrease in the overall administrative burden in 2016 compared to 2014, even though this was the time in which Serbia made the unprecedented leap in its history in the DB rankings.

Table 2: Results of Serbia in selected benchmarks

	2012	2013	2014	2015	2016	2017	2018	2019
<b>DB rank</b>	92	86	93	91	59	47	43	48
<b>GCR</b>	2.4	2.3	2.2	2.2	2.4	2.4	2.6	2.8
<b>SCM</b>	3.5	-	3.46	-	3.26	-	-	-

Source: *Doing Business* (2012-2019) Global Competitiveness Report, and Business Enabling Project

### FULL AND PARTIAL REGULATION IMPLEMENTATION: "WE'RE NOT IN KANSAS ANYMORE"

Living in countries in transition, one often encounters a proverb that "good laws are not the problem, but their actual implementation in practice". This statement is not only uttered in circles of political or NGO activists, but also in those of legal scholars and business people and are even written into EU progress reports or other publications that cover the legal or business environment in respective countries. This lackluster implementation of rules and regulations stems mostly from weak institutions and the absence of rule of law, due to the political control that governments and other important stakeholders exert over judiciary and civil services. In transition countries, this may be legacy of the authoritarian regimes before the 1989 that kept a firm grip on all three branches of power, including over media and the economy as a whole, but also of different political views of constituencies in these countries, compared to Western Europe, or even cultural differences.

This different situation regarding the way in which judiciary and civil service operate in countries in transition compared to other advanced economies is clearly visible when international benchmarks that measure corruption perception, rule of law, and government effectiveness are taken into account.

#### **RULE OF LAW**

*Oxford English Dictionary* defines 'rule of law' as "the authority and influence of law in society, especially when viewed as a constraint on individual and institutional behavior; (hence) the principle whereby all members of a society (including those in government) are considered equally subject to publicly disclosed legal codes and processes". In the case of business environment, the presence of rule of law would entail that all business entities are subject to the same

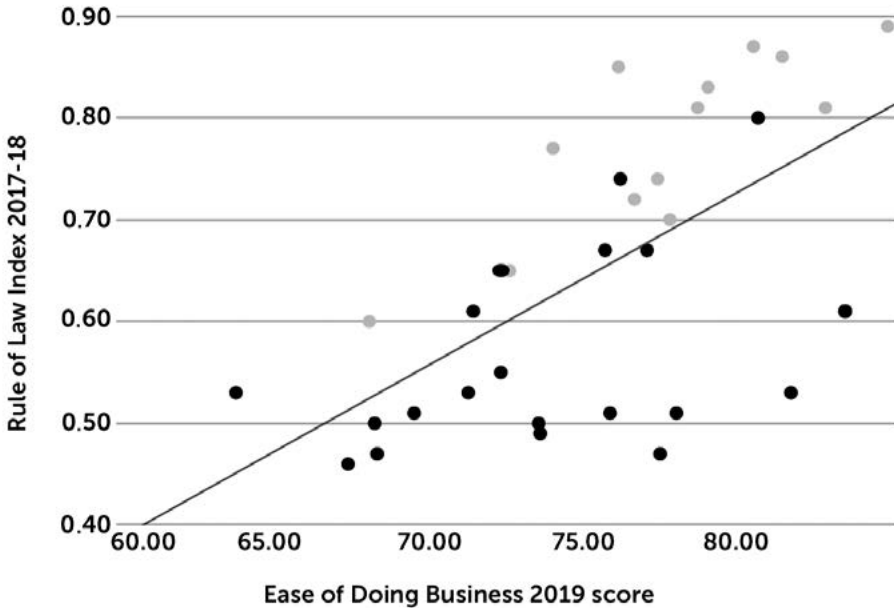


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rules and regulations, no matter who their owner/manager may be. However, partial implementation of business regulations in practice can be often used to gain competitive advantage – for example, if the authorities turn the blind eye should a selected company not implement costly regulations, while they are very efficient in making other companies follow these rules. This situation does not cover the cases in which regulations are discriminatory per se, as long as they apply to all entities, which can also advance the interests of those with ties to high-ranking government officials, as in the recent cases of working hours regulations of retail store chains in Poland, which favored small local shops in domestic ownership over big retail chains mostly in foreign ownership, and trade unionists.

Figure 1 shows the connection between *Doing Business 2019* score of the World Bank and the *Rule of Law Index 2017-18* of the World Justice Project. Transition countries are in black, while the EU15 are in gray. Notice that there is a clear connection between



Figure 1: *Doing Business* versus *Rule of Law Index*

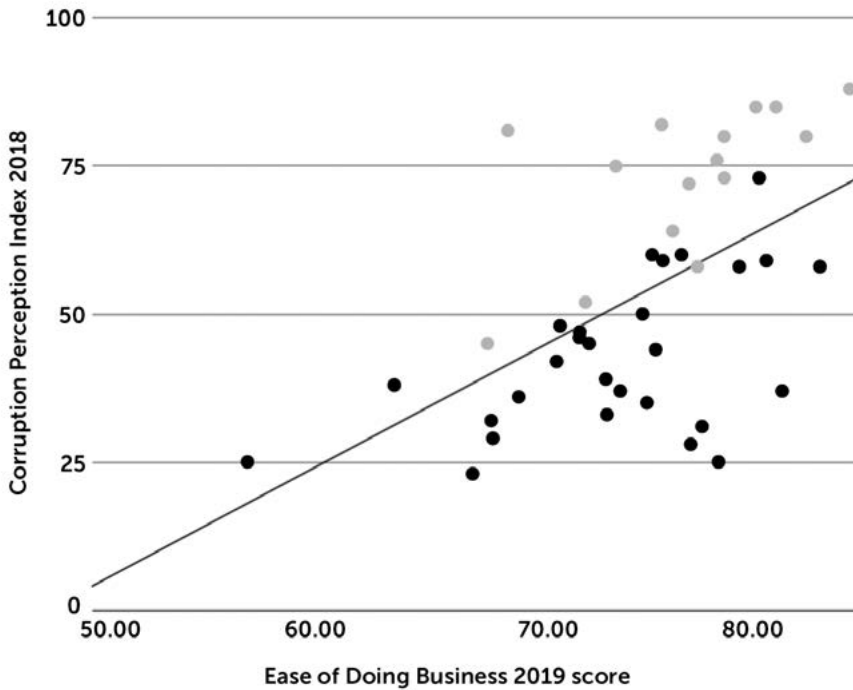
these two variables, although on a small sample (the Pearson correlation coefficient being 0.63), but that most transition countries have a much lower score in the rule of law segment than would be expected by their DB score alone.

### **CORRUPTION**

A similar situation is also visible in the field of corruption. On average, countries in transition report a higher perception of corruption compared to their EU15 counterparts. Figure 2 shows the connection between the *Corruption Perception Index* (CPI) of the Transparency International and the *Doing Business* score (once again, EU15 in gray, and transition countries in black). There is a strong correlation between these variables (correlation coefficient of 0.56), but once again most transition countries score better on the DB than would be expected on their CPI results alone.



VIEWING BUSINESS ENVIRONMENT IN THE NATIONAL CAPITAL ONLY AS A PROXY FOR BUSINESS ENVIRONMENT IN THE WHOLE COUNTRY HAS ITS SHORTCOMINGS

Figure 2: *Doing Business* versus *Corruption Perception Index*

### GOVERNMENT EFFECTIVENESS

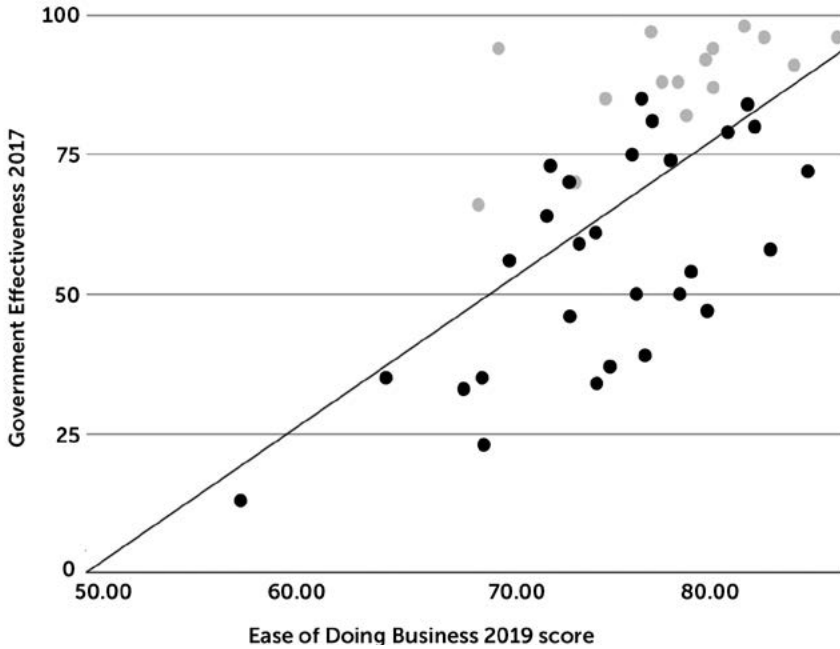
Once again, we face a similar situation [See Figure 3]. When government effectiveness data from the *World Governance Indicators* (WGI) of the World Bank are considered, we encounter once more a similar pattern: countries in transition (in black) have on average a lesser degree of government effectiveness than the EU15, but also many of them have higher DB score than their governance indicators would make us suspect.

These three small overviews of the *Doing Business* scores for transition countries all point to the same conclusion, that the DB scores in some transition countries are significantly inflated, since these scores are not followed by high scores in rule of law and government effectiveness, as well as low perception of corruption.

### REGIONAL DISPARITIES IN REGULATORY ENVIRONMENT: 50 SHADES OF GRAY

One of the reasons why the *Doing Business* report should be taken with caution in all countries it covers is due to the existence of regional disparities. The DB is calculated on the basis of data coming from the biggest city in the country (usually the nation's capital) and only in the cases of the most populous countries (such as China, Russia, India, the United States etc.) data from the second biggest city in the country is also used. This brings out the question whether the situation in the nation's capital or its most populous city is a good representation for the situation in the country as a whole.

A partial answer may be derived from the DB data itself, since there is special research regarding regional regulatory environment

Figure 3: *Doing Business* versus “Government Effectiveness”, World Governance Indicators

in some countries. Over the years, these special surveys were implemented in seventeen countries, as well as in two stand-alone publications covering seven more countries, but not all of them had the aggregated DB rank calculated. Therefore, the national ease of doing business was calculated for thirteen countries in total.

These data show mixed results: in countries such as India, Pakistan, Spain, Colombia, and Czechia, capital cities have better business regulation than the country average, while in Russia, Poland, Mexico, Kazakhstan, Croatia, Portugal, and Slovakia the capital city fares worse than the national average. This disparity shows that viewing business environment in the national capital only as a proxy for business environment in the whole country has its shortcomings since administration resources and quality can vary substantially between different parts of a country.



MORE BUSINESS-FRIENDLY REGULATION HAS A POSITIVE EFFECT ON ECONOMIC ACTIVITY, AND THE DB CAN GRASP REGULATORY CHANGES AND EVALUATE THEM

## IS DOING BUSINESS STILL RELEVANT?

After having a look at these problems, one question arises: Is the *Doing Business* report still relevant for describing the business environment in a country? It depends on the way it is used. The DB is still useful, but – as mentioned above – it has to be used with a grain of salt.

For example, the introduction of a new procedure for obtaining a construction permit in Serbia, whose implementation began in January 2016, led to a significant increase in the total number of licenses that were given. After the 2008 recession, the number of new building permits soared to half of its pre-crisis peak [See Figure 4] and remained at this level for several years. It started slowly growing in 2015, when the first waves of deregulation in this area began, but it truly bore fruit the next year.

This soar in building activities was mostly due to the excess liquidity stemming from the European Central Bank's monetary policy, but these resources would not have been employed in the real estate construction had it not been the regulatory loosening that allowed it, by cutting red tape and lowering costs. In order to do so, the government in Serbia decreased the number of procedures from 16 to 11, the time in days from 264 to 110, and total costs as a percentage of the object from 25.7% to only 1.8%. Serbia thus earned the 11<sup>th</sup> place in the DB 2019, after its deplorable 186<sup>th</sup> place it had in the DB 2015. As may be seen, more business-friendly regulation has a positive effect on economic activity, and the DB can grasp regulatory changes and evaluate them.

Nevertheless, at the same time, although the DB does provide a good brief overview of the key business legislation in a country at stake, it is not enough to make a good nuanced view of the whole regulatory framework and its actual implementation in prac-



THE DB SCORES IN SOME TRANSITION COUNTRIES ARE SIGNIFICANTLY INFLATED, SINCE THESE SCORES ARE NOT FOLLOWED BY HIGH SCORES IN RULE OF LAW AND GOVERNMENT EFFECTIVENESS, AS WELL AS LOW PERCEPTION OF CORRUPTION

tice, since it implies high standards in rule of law, which may not really be in place.

One of the best examples of the low level of rule of law in Serbia is the Savamala affair, that took place in May 2016. Under the cover of the night, a group of masked men demolished a quarter in the center of Belgrade, razing down a group of business buildings using heavy machinery. They even kidnapped passers-by as potential witnesses, and employees, and were assisted by the local city utility companies which cut the power while both the national and community police did not respond to calls of citizens in distress, stating that this is not

their jurisdiction. After a couple of days, this now cleared land was given through legal appropriation to a controversial residential building project, Belgrade Waterfront. After a wave of citizen protests, Prime Minister Aleksandar Vučić accused top city authorities as culprits.

However, no one was ever tried for this crime, the Prosecutor's Office is still managing the introductory investigation, and the mayor is now the Minister of Finance. This affair even earned a resolution of the Euro-

pean Parliament, which asked for its swift resolve and penalties for the perpetrators, but this all fell on deaf ears. No matter how efficient the process of obtaining a building permit is, if affairs such as Savamala happen, it means that business environment in the country at stake is a far cry from being business friendly. In cases like these, the DB can provide a false picture of the situation.

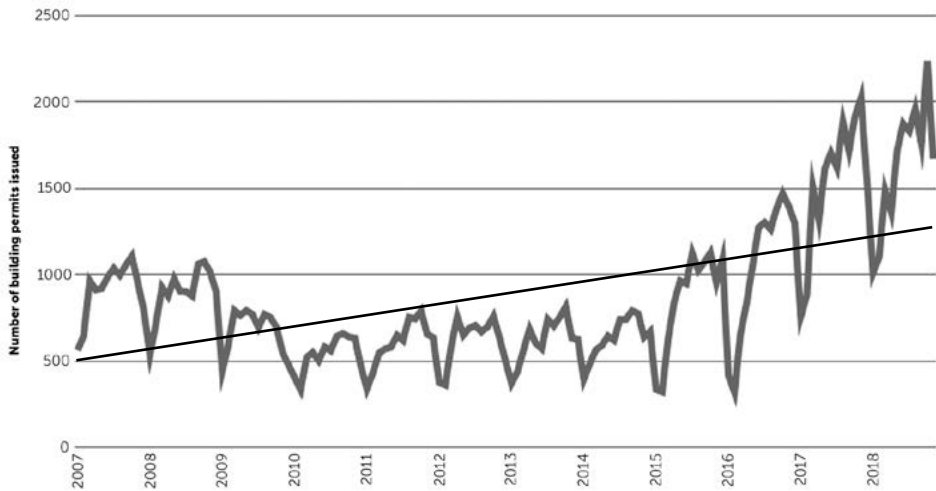
In order to account for its weak points, the *Doing Business* report should therefore be accompanied with other important interna-

Table 3: Subnational *Doing Business* scores

Country	Data reference	No. of cities	Rank of the capital
Morocco	DB 2008	8	-
India	DB 2009	17	6
Pakistan	DB 2010	13	4
Russian Federation	DB 2012	30	30
Spain	DB 2015	19	2
Poland	DB 2015	18	17
Mexico	DB 2016	32	31
Colombia	DB 2017	32	3
Kazakhstan	DB 2017	8	8
Croatia	DB 2018	5	4
Czechia	DB 2018	7	1
Portugal	DB 2018	8	6
Slovakia	DB 2018	5	5

Source: World Bank (2009-2018) *Doing Business Subnational Reports*. Available [online]: <http://www.doingbusiness.org/en/reports/subnational-reports>

Figure 4: Number of construction permits in Serbia [2007–2018, monthly]



Source: Serbian National Statistical Office. Available [online]: <http://www.stat.gov.rs/en-US>

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ONE OF THE REASONS WHY THE DOING BUSINESS REPORT SHOULD BE TAKEN WITH CAUTION IN ALL COUNTRIES IT COVERS IS DUE TO THE EXISTENCE OF REGIONAL DISPARITIES

tional measures. These should be benchmarks that evaluate business regulation – such as Global Competitiveness Report, Economic Freedom in the World or *Index of Economic Freedom* – but also those that evaluate the level of rule of law and corruption. Only such a broader view of the whole regulatory environment can really inform us about the character of the business regulation in a given country. ●



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