

Revival of SMEs in the spotlight!

Besides corporations, small and medium-sized enterprises (SMEs) play a fundamental role in economies worldwide. Given their size, their adaptability brings them a number of advantages but also often limits them. In response to this situation, governments tend to implement measures that should help SMEs fight their handicaps.

EU's efforts to put SMEs back on track

Today, there are no doubts about the significance of SMEs in national economies. In the Slovak Republic, SMEs represent almost 99.9% of all businesses (Chart 1). They provide approximately 72% of private sector jobs for the active labor force and almost 60% of jobs in the whole economy. They contribute by more than 50% to the added value created.

The majority of SMEs represent micro enterprises which hire a small number of employees; they are often categorized as family owned businesses or "one-man show" enterprises owned by a private individual.

Regardless of their size, SMEs have to fulfill the same obligations as large companies, which manage incomparable amounts of capital and resource capacities. Entry into the market for SMEs is often accompanied by red tape; doing business itself is influenced by a number of regulatory and administrative barriers. The regu-

latory framework is unstable and is constantly changed without sufficient analysis of its impact on the private sector (regulatory impact assessment), etc.

Moreover, also as a result of the above-mentioned barriers, most Europeans prefer the career path of an employee in an established business than of an entrepreneur. This is seen more and more often. As the European Commission (EC) survey presents (Chart 2), the share of people preferring self-employment to being an employee is dropping in most of the EU member states. Self-employment is generally more popular among non-EU countries.

That's why public administrations in Europe, but also in the US or Asia, tend to implement a wide range of measures that should help SMEs combat their handicaps – on one side by streamlining the business environment, and on the other side by implementing various incentives.

Globally, there may be many

reservations towards the EC or its mission to create "a single Europe." However, it is hard to deny that the EC pays close attention to the problems of SMEs and tries to revive entrepreneurship in Europe.

In 2008, the EC presented its long-term agenda called the "Small Business Act" (SBA) which constitutes a flagship of policies to support SMEs across Europe. The SBA summarizes all previous and current activities of the EU and its member states and identifies the problems that SMEs face.

At the same time, the SBA provides a list of recommendations with the aim to eliminate current barriers and to setup an "ideal" business environment. These recommendations are formulated in a set of ten principles that cover particular topics of the SBA (e.g. fostering entrepreneurial interest, getting a second chance in doing business, simplifying the existing regulatory environment, promoting e-government and one-stop-shop solutions, using benefits of the Single Market as well as the

growing market outside of the EU, etc.). One of the ten principles, 'Think Small First,' is of extra importance in terms of SMEs. The 'Think Small First' principle requires a SME-friendly approach by legislation. A range of tools are identified to ensure the effective implementation of this principle, including the application of an "SME test" for forthcoming legislative proposals, use of SME-specific provisions in legislation to avoid inadequate regulatory/administrative burden on SMEs, consultation of SME stakeholders, etc.

All of these EC actions are based not only on the European experience and the best practices of particular member states, but extensively inspired by models from the main competitors, for example the US began systematically supporting SMEs since the Great Depression.

How about Slovakia?

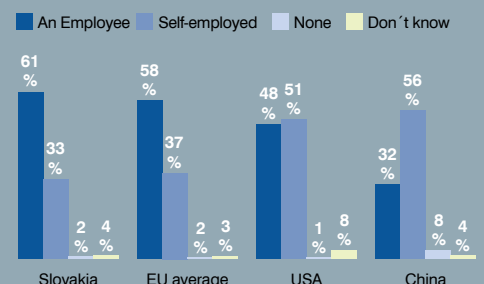
Changes in the Slovak business environment are reflected in the quantitative characteristics of the SME sector. In 2012, for the first time, the Slovak Statistical Office recorded a decline in the total number of SMEs. This historic drop (year-to-year by 0.7%, which amounts to 4,000 entities) may be associated with lower growth of the Slovak economy, low household consumption, as well as with insufficient steps taken to improve the conditions for doing business.

Chart 1: The size structure of the business sector in the Slovak Republic and EU Business

		SIZE OF ENTERPRISE					SMEs	Total
		Micro	small	medium	large			
		(0-9)	(10-49)	(50-249)	(250+)			
EU - 27 (2010)	Number of businesses in non-financial business economy, 2009 (in thous.)	20,154	1,355	222	42	21,731	21,773	
	Share in the number of businesses	92.6%	6.2%	1.0%	0.2%	99.8%	100.0%	
Slovakia (2012)	Number of businesses	535,834	13,121	2,653	615	551,608	552,223	
	Share in the number of businesses	97.0%	2.4%	0.5%	0.1%	99.9%	100.0%	

Source: Data for the Slovak Republic: SO SR, processed by NADSME. Data for the EU-27: Eurostat, Structural Business Statistics, sectors cover SK NACE Sections B through N and division 95, at the time of processing the material data were available for year 2010

Chart 2: What would you prefer to be?



Source: Survey - "Entrepreneurship in the EU and beyond", European Commission





Regarding this situation, it is necessary to underline that it is mostly SMEs, and especially the new ones, that continue to create jobs and thus contribute to Europe's recovery from the economic crisis. Based on EC data it amounts to approximately four million new jobs yearly.

From the business standpoint, Slovakia's situation may be characterized by three key points:

1. Low competitiveness

Slovakia is less competitive and has a less positive business environment when compared globally to other countries, which focus their efforts on improving their status quo. Slovakia is mostly stagnating in its approach to competitiveness, which is exemplified by a number of international rankings, for example 'Doing Business' by the World Bank or the Annual SBA Report assessing the country's SBA implementation. It has been approximately ten years since Slovakia was recognized as the "Tatra Tiger" in terms of concrete steps towards an improved business environment. Since then, not many progressive measures related to improving competitiveness have been taken. If we focus on the above-mentioned topic of preference between employment and entrepreneurship, in Slovakia the percentage is fairly

below the EU average.

According to the World Bank's ranking of global competitiveness, it is necessary to point out a sad fact, that only two out of the ten best performing countries are EU member states (Denmark and the United Kingdom).

2. Decline of SMEs

The long-term decline of SMEs, caused predominantly by the economic crisis, is also the outcome of inadequate attention paid by leaders. Here are a few examples:

As a result of external economic impacts and low competitiveness, SMEs are recently recording a reduction in their profitability (Chart 3). Overall only 56% of SMEs (legal entities) achieve positive economic results, while in the category of micro enterprises it is even less.

In addition, compared with the pre-crisis year of 2008, the average number of those employed in SMEs is lower by nearly 46,000.

Another issue is size reshuffling; between the years 2008 and 2012 there was a drop by 51% in the number of small and medium-sized enterprises. This means that due to elementary problems, Slovak SMEs have

only limited space for expansion, business development, implementation of innovations, and ability to increase the number of employees.

3. Slow implementation of the EC's agenda

The slow implementation of the SBA and the Entrepreneurship 2020 Action Plan into national policies influences the state of business environment in Slovakia too. According to the 2012 SBA Fact Sheet, Slovakia ranked below the EU average in applying the SBA recommendations. There was only one area out of ten in which Slovakia performed better than the EU average (which was using the benefits of the Single Market).

What is Slovakia missing to become a prosperous economy?

It is primarily a business friendly environment in which both start-ups and experienced entrepreneurs would benefit from a wide range of instruments to support their business ideas. Such an environment could also provide an opportunity for identified marginalized groups (women, seniors, youth, migrants, and handicapped) to participate in entrepreneurial activity. Failure in business should be perceived as an opportunity for repeated market entry and not automatically understood as a failure.

Secondly, the effective implementation of the regulatory impact assessment system, including the introduction of the so-called SME test might diminish regulatory burden and cut red tape.

Moreover, entrepreneurship should be accepted as a relevant career choice and receive support in the educational process. Building entrepreneurial competencies

at a young age might be utilized by both entrepreneurs as well as employees at a later stage.

Finally, efficient introduction of electronic communication between the public and private sectors would help lower the cost of sharing mandatory information for private businesses and also for the public sector when providing services to its customers.

Is a happy end coming?

In the last 20 years, the Slovak business environment experienced more ad hoc reforms than systematic improvement.

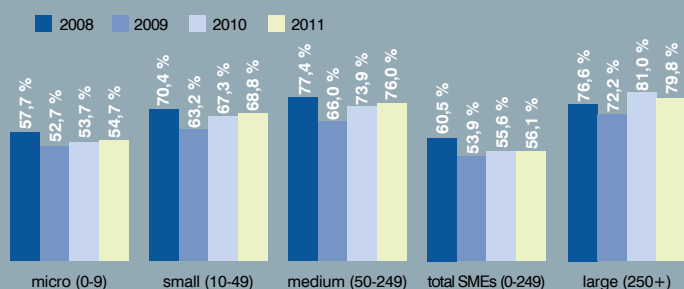
The new EU multiannual financial framework for 2014-2020 offers Slovakia a chance to support SMEs via a number of financial and non-financial instruments (loans, equity funding, regulatory impact assessment system implementation, mentoring services, incentives for marginalized groups, start-up promotion, one-stop-shop solutions, etc.) as defined in the national Operational Programs. This might be the time to formulate a clear SME strategy, a special Act on SMEs, utilizing the best EU and international practices in a long-term framework that would also accelerate the fulfillment of key SBA recommendations.

If it doesn't use this opportunity, Slovakia might experience a continuous degeneration of the SME sector, decline in competitiveness, and lag more and more behind countries that have understood the necessity of pro-SME policy.



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Chart 3: Share of enterprises with profit, by size categories



Source: Report on the state of Small and Medium Enterprises in the Slovak Republic in 2012, NADSME

