SME Policy Index

# Eastern Partner Countries 2024

## BUILDING RESILIENCE IN CHALLENGING TIMES



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# SME Policy Index: Eastern Partner Countries 2024

BUILDING RESILIENCE IN CHALLENGING TIMES

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# Foreword

We are pleased to present this fourth edition of the *SME Policy Index: Eastern Partner countries 2024*.

This Policy Index offers the latest findings on SME development and related policies in five partner countries (Armenia, Azerbaijan, Georgia, Republic of Moldova, Ukraine), and it also presents regional trends and country-specific analysis and recommendations.

This year's report arrives in a particular context, given the economic consequences of the COVID-19 pandemic and Russia's war of aggression against Ukraine, as well as the EU Membership applications in 2022 by Ukraine, the Republic of Moldova and Georgia. Small and medium-sized enterprises (SMEs) make a critical contribution to the economies and societies in the European Union and Eastern Partnership (EaP) countries. Across the Member countries of the OECD, SMEs account for more than 99% of firms, over 60% of employment and most of the value-added in the business sector. While SMEs significantly shape job market dynamics and influence economic growth, they are also a key source of innovation. Indeed, a thriving SME sector is critical for a competitive, diversified and resilient economy – one that can quickly adapt to major global trends such as demographic shifts, digitalisation, and the green transition.

Due to their more limited resources and their vulnerability to crisis, SMEs require clearly defined policy support in order to ensure their resilience to any future shocks and to unlock their full productive potential. This is particularly true for the EaP countries, given their greater exposure to the effects of Russia's invasion of Ukraine, coming on the back of the economic and social consequences of the COVID-19 pandemic. SMEs across the EaP countries represent over 98% of all firms and 60-80% of employment, yet they generate around half of the total value added of the business sector.

The SME Policy Index, which was first created in 2012, is applied to the EaP countries every four years. The Index is structured around the ten principles of the EU's Small Business Act for Europe (SBA) and incorporates the priorities laid out in the EU's SME Strategy for a Sustainable and Digital Europe and the OECD Recommendation on SME and Entrepreneurship Policy. As such, it is an important tool encouraging domestic economic reforms in countries wishing to integrate further with the European Union in the context of the EU enlargement policy. The methodology applied helps in assessing and monitoring progress, as well as identifying reform priorities for more effective, efficient and coherent SME policies by benchmarking against EU and OECD standards. A new pillar was added to the methodology in 2024, which analyses policies in support of the digital transformation.

Altogether, the *SME Policy Index: Eastern Partner countries 2024* concludes that the EaP governments have continued to demonstrate their commitment to supporting SMEs through the introduction of various reforms conducive to stable and strong business environments. Partner countries have built on the recommendations presented in the 2020 edition to improve their policy settings, albeit at different speeds and in the context of very specific challenges over the last four years. All five governments have taken important steps to provide more and better e-government services, while entrepreneurial learning is becoming increasingly common in school curricula. Opportunities to strengthen SME skills have also greatly improved. Some countries have developed dedicated programmes for the digital and green transition of the SME sector.

While significant improvements are evident, more remains to be done.

First, regulatory frameworks should be updated regularly, including through new approaches to industrial policy and through the adoption of emerging digital, environmental, social and governance standards. Conclusions from the new methodological pillar on the digital economy for SMEs point to a substantial need for support as, for example, only 57% of small firms in the EaP region have a company website versus 84% of large firms. Meanwhile, just 32% use social media, compared with 70% of larger firms. Environmental, social and governance considerations are increasingly seen as important, but they rarely feature on any occasion of information sharing.

Second, to allow more ambitious technological adoption and boost innovation, policies must go further in enabling access to finance for SMEs, helping diversify sources of finance, reducing dependence on debt, capitalising on emerging digital trends that could broaden financial access – and working to boost financial skills in SMEs. In the EaP region, the estimated financing gap for SMEs is substantial, as a 200% increase in lending would be needed to meet the needs of SMEs fully.

Third, monitoring and evaluation practices remain limited in EaP countries, and better data collection frameworks will be needed to capture the impact of policies on firms.

Finally, more targeted measures supporting the ability of SMEs to trade and integrate into global value chains could greatly benefit EaP countries, given their relatively small domestic market sizes.

We commend the governments of Armenia, Azerbaijan, Georgia, the Republic of Moldova and Ukraine for their determination to improve the policy environment for SMEs, and we look forward to continuing our joint effort in designing and implementing better policies that foster a successful transition to more productive, sustainable and inclusive business environments in Eastern Partnership countries. This will boost investments and economic development and benefit the people of the region.

The close involvement of EaP governments throughout greatly improved the report, which is the result of a collaborative effort by the Organisation for Economic Co-operation and Development (OECD) and the European Bank for Reconstruction and Development (EBRD), with the support of the European Commission (EC), the European Training Foundation (ETF), and the United Nations Economic Commission for Europe (UNECE). The views of a wide range of stakeholders, including SMEs themselves, were sought and are reflected throughout the publication



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The report was written under the guidance of Andreas Schaal, Director of OECD Global Relations and Co-operation, and William Tompson, Head of the OECD Eurasia Division.

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# Abbreviations and acronyms

| | |
|---|---|
| ARMSTANDARD | National Body for Standards and Metrology (Armenia) |
| ASAN | Azerbaijani Service and Assessment Network |
| BDS | business development services |
| CA | conformity assessment |
| CAERC | Center for the Analysis of Economic Reforms and Communications |
| CM | comparable methodology |
| DigComp | EU Digital Competence Framework |
| EaP | Eastern Partnership |
| EBRD | European Bank for Reconstruction and Development |
| EEPO | Entrepreneurship and Export Promotion Office (Ukraine) |
| EIF | Enterprise Incubator Foundation |
| FDI | foreign direct investment |
| GNI | gross national income |
| GVC | global value chain |
| HEI | higher education institution |
| HPSU | high-potential start-up (Ireland) |
| IAF | International Accreditation Forum |
| ICA | Investment Council of Armenia |
| ICT | information and communications technology |
| IDDA | Innovation and Digital Development Agency |
| ILAC | International Laboratory Accreditation Cooperation |
| KOBIA | Kiçik və Orta Biznesin İnkişafı Agentliyinə, or SME Development Agency (Azerbaijan) |
| KPI | key performance indicator |
| M&E | monitoring and evaluation |
| MoHTI | Ministry of High-Tech Industry (Armenia) |
| MoJ | Ministry of Justice |
| MoU | memorandum of understanding |
| MSMEs | micro, small and medium-sized enterprises |
| ODA | Organisation for the Development of Entrepreneurship (Moldova) |
| PPD | public-private dialogue |

| | |
|---|---|
| PPL | Public Procurement Law |
| R&D | research and development |
| RIA | regulatory impact assessment |
| SEDS | Socio-economic Development Strategy of the Republic of Azerbaijan 2022-2026 |
| SMEs | small and medium-size enterprises |
| STEM | science, technology, engineering and mathematics |
| VET | vocational education and training |
| y-on-y | year on year |

# Executive summary

Over the last four years, the five countries of the Eastern Partnership (EaP) – Armenia, Azerbaijan, Georgia, the Republic of Moldova and Ukraine – have experienced major socio-economic and political shocks, above all the COVID-19 pandemic and Russia's war of aggression against Ukraine. The outbreak of the pandemic in early 2020 caused an unprecedented health crisis, with a spike in mortality estimated at close to 320 thousand excess deaths across the region. EaP governments issued stay-at-home orders, restricting mobility, social interactions and economic activities to contain the spread of the virus and rolled out important fiscal stimulus measures to mitigate the economic impact of the pandemic on households and businesses. Nevertheless, a large economic contraction occurred across the region, with EaP economies contracting between -3.8% and -7.2% of GDP in 2020.

As EaP economies rebounded, the war in Ukraine put the region at the epicentre of another shock in February 2022, which caused a significant slowdown in global growth and severely challenged the trajectory of economic recovery in the region. For Ukraine, the war represents a human tragedy on a scale not seen in Europe in decades, with tens of thousands dead and millions of refugees escaping or being internally displaced. Ukraine's productive capacity and trade relations have been devastated, causing GDP to fall by around 29% in 2022. Direct spillovers from the war also affected Moldova heavily via a large influx of refugees, an energy crisis and soaring inflation. By contrast, economies in the South Caucasus have performed better than expected in 2022, due to high prices and global demand for hydrocarbons (Azerbaijan), and a significant influx of mostly skilled labour from Russia providing a short-term boost to domestic consumption and workforce development (Armenia, Georgia).

Against this challenging backdrop, supporting the development of small and medium-sized enterprises (SMEs) has become more important than ever to building more resilient and sustainable EaP economies. Crucial job creators, flexible innovators and the largest group of business entities, SMEs can serve as engines of economic transformation and a major channel through which the local socio-economic fabric adapts to global trends. In EaP countries, SMEs represent over 98% of enterprises, 60-80% of employment (except for Azerbaijan) and around half of total value added. However, most SMEs in the region are subsistence micro-entrepreneurs operating in low-value-added sectors and with limited propensity to export, so their potential to act as agents of growth and innovation remains largely untapped and calls for renewed efforts to create a better policy environment for new business creation, growth, innovation, and internationalisation.

This edition of the SME Policy Index shows how SME policy frameworks have evolved across the EaP region since the beginning of 2020. It provides an updated assessment of progress along twelve policy dimensions, as well as a description of country-specific challenges and recommendations for further reform. For the first time, the assessment includes an analysis of policies for the digital transformation of SMEs, which is vital to building a stronger and more resilient SME sector, especially since the COVID pandemic pushed many firms online for the first time to experience first-hand the value of digital technologies.

While country-specific challenges and suggested reforms are outlined in detail in the following chapters, this report identifies some key recommendations that are relevant across the EaP region:

- **Further enable and support the digital transformation of SMEs.** Business digitalisation requires governments to work both on broad, fundamental enabling factors for the development of the digital economy, as well as on providing specific support measures for SMEs. On the former, EaP countries should prioritise enhancing broadband connectivity to address remaining digital divides across individuals and firms, and step-up their efforts to build digitally literate societies by promoting the development of digital skills at all education levels and as part of lifelong learning. On the latter, EaP governments should design dedicated initiatives to support SME digitalisation, encompassing both the adoption of digital technologies and the development of a digital culture inside firms, while also raising awareness for the importance of digital security.
- **Continuously update the institutional setting for SME policies, taking into consideration each country's specificities.** Medium-term strategic frameworks for SME policy, developed in consultation with a multitude of stakeholders, offer governments an important compass to identify emerging challenges for SMEs and to design targeted solutions to address them. Regularly updated action plans with clearly identified costs and implementation responsibilities empower institutional actors and provide certainty about the resources available. Different models can emerge for SME agencies to manage the delivery of support services for SMEs: smaller countries with a relatively limited community of support service providers may choose to have a strong role in the direct management and delivery of support programmes, while larger countries with a vibrant community of non-governmental service providers could opt for a more decentralised approach, acting as a platform and leveraging the capabilities of other actors in the ecosystem.
- **Ensure that SMEs have access to key resources to start, develop and grow their businesses.** As access to finance remains a challenge for SMEs, EaP governments should work to ensure that smaller firms are not disproportionally penalised by their size-related factors. This entails, for instance, improving enforcement conditions for secured transactions to lower the overall risk and cost of lending and enforcement processes, or establishing support mechanisms for developing growth stage funding for start-ups, since the venture capital industry in the region is still in its infancy. Similarly, EaP countries should encourage the development of an entrepreneurial mindset throughout society, creating conditions in which individuals are more likely to start a business based on an identified opportunity than because of a lack of alternative employment options. Embedding entrepreneurship in school curricula and deepening the co-operation between schools and SMEs could help, as would complementary efforts to help SMEs enhance the skills of their managers and employees in response to changing labour market needs. Finally, EaP governments could promote SME access to and participation in public procurement by improving e-procurement options and building the skillset of procurement officers in contracting authorities.
- **Develop regulations in an SME-friendly and competitive manner, responding to emerging trends.** Legislative simplification should remain a priority and regulatory policy should be mindful of the potential impact of new regulations on SMEs. To this end, EaP countries should prioritise the implementation of regulatory impact assessment procedures with the adoption of "SME tests" specifically conceived to evaluate the likely consequences of new policies on smaller firms. This is key to design effective regulatory environments, ranging from taxation to environmental regulations. Similarly, the emergence of a new set of digital financial services calls for a regulatory and supervisory approach based on multi-stakeholder consultations, as well as dedicated skills and resources (e.g., sandboxes, innovation offices) to address the related challenges.
- **Sustain SME competitiveness through the entire life cycle of the business**. Governments in EaP countries have done much to simplify the operational environment for SMEs, in particular when it comes to opening a business and offering e-government services. Entrepreneurial risk-taking could be further encouraged by creating more efficient and predictable insolvency and second chance frameworks allowing honest entrepreneurs who have gone bankrupt a fresh start. Productivity levels, however, remain generally low and demand a constant improvement of the human and technological capital employed by firms. For SMEs, often constrained by lack of

knowledge, time, and resources, EaP governments should further refine their support programmes aimed at increasing their access to training opportunities, managerial advice, as well as dedicated financial tools to invest in new equipment, experiment with new technologies, and sustain the extra costs to enter new markets. This is particularly relevant to ensuring that SMEs are not left behind in the transition to more digitalised and greener economies.

- **Consolidate monitoring and evaluation frameworks for more robust evidence-based policy making.** While governments in EaP countries have embraced regular monitoring practices of their broad SME policy documents and initiatives, rigorous evaluations of their impact on actual SMEs' economic performance remain very rare. As a first step, embedding clear and measurable key performance indicators in the policy cycle through publicly available policy documents would allow for a transparent reporting of governments' activities against their own targets. Furthermore, detailed analyses using more granular, firm-level data comparing beneficiaries' performance against valid control groups would allow to gauge the impact of the support provided on the performance of participating companies. The information thus generated would also be key to estimating the economic additionality of the specific support programmes and could feed back as an important input for their future adjustments. Finally, nationwide outcome-oriented statistical indicators, regularly produced by the statistical offices, would also offer a broader view of how public policies are impacting different thematic dimensions of the performance of the business sector (e.g., innovation, environmental, internationalisation).

# 1 Policy framework, structure of the report and assessment process

## Policy frameworks underpinning the SME Policy Index

The SME Policy Index is a benchmarking tool for assessing and monitoring progress in the design and implementation of policies for small and medium-sized enterprises (SMEs). The index was developed in 2006 by the OECD in partnership with the European Commission, the European Bank for Reconstruction and Development (EBRD) and the European Training Foundation (ETF). Since then, it has been implemented across a growing geographical area that now covers almost 40 economies in 5 regions: the Eastern Partnership (EaP), the Western Balkans and Turkey, the Middle East and North Africa, the Association of Southeast Asian Nations (ASEAN), and Latin America and the Caribbean.

For the Eastern Partner countries,[1] this edition of the SME Policy Index draws on the guiding principles identified by the OECD's *Recommendation on SME and Entrepreneurship Policy*, notably with regards to its principle 5 on the Digital transformation of SMEs (OECD, 2022[1]). It also embraces the priorities laid out in the EU's SME Strategy for a Sustainable and Digital Europe and is structured around the ten principles of the EU's Small Business Act for Europe (SBA), which provides a policy framework to improve SME competitiveness and promote entrepreneurship (Box 1.1).

While there are a number of other assessments of the business environment in EaP countries, the SME Policy Index adds value through its holistic approach to SME development policies, providing policy makers with a single window through which to observe progress in their specific areas of interest. Over the years, the SME Policy Index has established itself as a change management tool used by participating national governments to identify priorities and obtain references for policy reform and development.

The SME Policy Index is implemented within the EU4Business initiative. EU4Business is an umbrella initiative that covers all EU support for SMEs in the Eastern Partnership region. It breaks down barriers SMEs face in their progress – such as limited access to finance, burdensome legislation and difficulties entering new markets – using finance, support and training to help them realise their full potential. EU4Business support is delivered together with other organisations such as the EBRD and the European Investment Bank (EIB).

### Box 1.1. The Small Business Act and the SME Strategy: key policy tools for EU Member States

**The Small Business Act for Europe (SBA)**

Adopted in June 2008, the SBA reflects the EC's recognition of the central role of SMEs in the EU economy. It aims to improve the approach to entrepreneurship in Europe, simplify the regulatory and policy environment for SMEs, permanently anchor the "Think Small First" principle in policy making, and remove the remaining barriers to SME development. Built around ten principles and several concrete policy actions to implement them, the SBA invites both the EC and the EU Member States to tackle the obstacles that hamper SMEs' potential to grow and create jobs.

**The SME Strategy for a sustainable and digital Europe**

Presented in March 2020, the "SME Strategy for a sustainable and digital Europe" aims to contribute to the objectives of the European Green Deal, the Digital Decade, and other EU actions launched in the context of the twin digital and green transition, namely achieving a climate-neutral, resource-efficient, and agile digital economy by mobilising the potential of SMEs. To do so, the strategy puts forward actions based on the following three pillars: i) Capacity-building and support for the transition to sustainability and digitalisation; ii) Reducing regulatory burden and improving market access; and iii) Improving access to financing.

The strategy builds on the very strong foundations of the EU's existing SME policy framework and support programmes, notably the 2008 Small Business Act, the 2016 Start-up and Scale-up Initiative, the programme for the Competitiveness for Enterprises and SMEs (COSME), and SME support actions funded under the Horizon 2020 programme and the European Structural Investment Funds.

**The SME performance review**

The SME Performance Review is one of the main tools used by the European Commission to monitor and assess countries' progress in implementing the SBA. The review brings in comprehensive information on the performance of SMEs in EU Member States and other countries participating in the EU's dedicated programme for SMEs – COSME. It consists of two parts: an annual report on European SMEs, and SME country fact sheets. The SME fact sheets present an assessment of the progress in the implementation of the EU SME Strategy and the SBA at national level. They focus on key performance indicators and national policy developments related to SME policy.

Source: (European Commission, 2008[2]); (European Commission, 2020[3]); (European Commission, 2023[4]).

Building on the strengths of the Index and in order to address some of its weaknesses (Table 1.1) and increase its impact, this 2024 edition goes beyond the analysis of areas covered by the SBA to capture emerging economic and policy trends and priorities (i.e. digitalisation), strengthen the link between policies and economic outcomes, and finally safeguard comparability with previous SBA assessments (see Annex A, "Methodology for the Small Business Act assessment", for more information on the 2024 methodology update). Thus, the 2024 SME Policy Index includes:

- a new pillar assessing selected framework conditions for the digital transformation
- extended and amended sub-dimensions to collect relevant information
- increased focus on countries' ability to collect statistical information on outcome-oriented indicators.

### Table 1.1. SME Policy Index strengths and weaknesses

| Strengths | Weaknesses |
|---|---|
| Focuses on a specific region where shared history, culture and geography allow for more relevant benchmarking between countries. | Within-country differences (e.g. differences in the level of SME activity in capitals and regions) may not be adequately captured in the analysis. |
| Takes a participatory approach to evaluation and measurement that brings together government stakeholders, the private sector and partner organisations. | As the same set of indicators and weights is applied to all countries of the region, certain country-specific characteristics might not be given full consideration in the scoring. |
| Independent and rigorous assessment enables it to benchmark the performance of EaP countries against EU and OECD standards. | The weighting system for the sub-dimension scoring is based on expert opinion and therefore involves subjectivity. |
| Comprehensively evaluates the SME policy environment around the ten key principles of the Small Business Act for Europe. | Ensuring effective measurement of implementation and outcomes of government policy remains a challenge despite continuous work on methodology to address this issue.* |
| Uses country context and broader factors affecting SMEs and policy developments to complement the analysis reflected in the scores. | Remaining gaps in national statistics on SMEs in the EaP region and some divergence in definitions of SMEs undermine the comparability of data across countries. |
| Provides guidance on how to improve policy frameworks through good-practice examples and country-level policy recommendations. | |

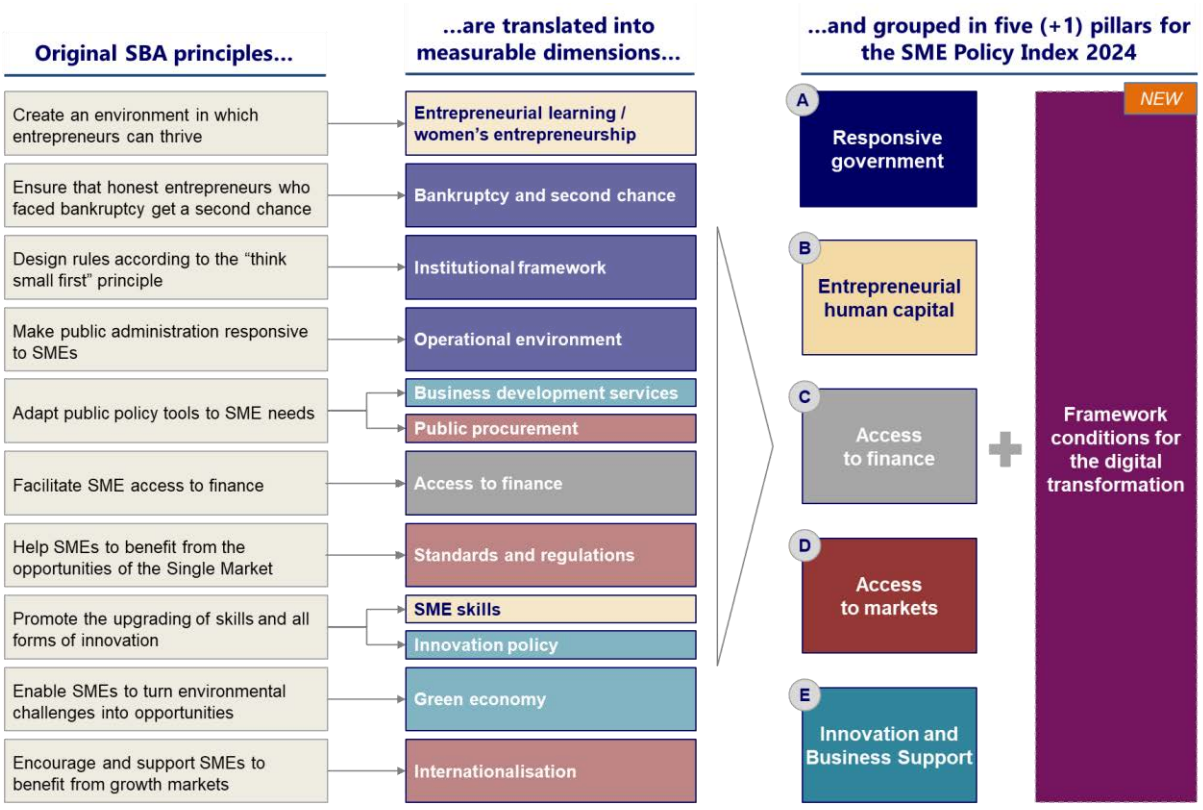
* See Annex A for more information on the 2024 methodology update.

## The 2024 assessment framework and structure of the report

The SME Policy Index links the 10 SBA principles to 12 measurable dimensions, which are further broken down into sub-dimensions and thematic blocks, each of which captures a number of indicators (Figure 1.1). The results of the SBA assessment are structured around five thematic pillars, as well as an additional pillar on selected framework conditions for the digital transformation specifically introduced for this round of assessment. Each pillar deals with core questions worthy of governments' attention when designing policies conducive to SME development:

- **Responsive government**: Is the overall operational environment conducive to business creation and risk-taking? Is the framework for SME policy responding to the needs of small and medium entrepreneurs?
- **Entrepreneurial human capital**: Are the formation of entrepreneurship key competence and the development of SME skills part of the public policy setting? Are they approached in a gender-sensitive way, supporting women's entrepreneurship?
- **Access to finance**: How available is external financing for start-ups and SMEs? Have specific policy instruments been introduced to make it easier and cheaper for small businesses to obtain funds to start and grow their businesses?
- **Access to markets**: Are SMEs able to sell their products and services to clients in domestic and foreign markets? Can public policies make it easier for small businesses to enter new markets?
- **Innovation and business support**: Can SMEs obtain advice and technology to remain competitive and increase their productivity? Is the government fostering a more innovative SME sector?

## Figure 1.1. Structure of the SME Policy Index 2024




These 12 policy dimensions are further broken down into 37 sub-dimensions capturing the pivotal policy elements in each area (Table 1.2).

## Table 1.2. Detailed SBA assessment framework and its link to the Small Business Act principles

| Small Business Act principle | SME Policy Index dimension | Related sub-dimensions |
|---|---|---|
| 1. Create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded | 1. Entrepreneurial learning and women's entrepreneurship | Entrepreneurial learning |
| | | Women's entrepreneurship |
| 2. Ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance | 2. Bankruptcy and second chance for SMEs | Preventive measures |
| | | Survival and bankruptcy procedures |
| | | Promoting second chance |
| 3. Design rules according to the "think small first" principle | 3. Institutional and regulatory framework for SME policy | Institutional framework |
| | | Legislative simplification and regulatory impact analysis (RIA) |
| | | Public-private consultations |
| | | Institutional settings for SME digitalisation |
| 4. Make public administrations responsive to the needs of SMEs | 4. Operational environment for SMEs | E-government services |
| | | Business licensing |
| | | Company registration |
| | | Tax compliance procedures for SMEs |
| 5. Adapt public policy tools to SMEs' needs: facilitate SMEs' participation in public procurement and better use State aid possibilities for SMEs | 5a. Business development services | Support services provided by the government |
| | | Government initiatives to stimulate private business support services |
| | | Business support services for the digital transformation of SMEs |
| | 5b. Public procurement | Public procurement |

| Small Business Act principle | SME Policy Index dimension | Related sub-dimensions |
|---|---|---|
| 6. Facilitate SMEs' access to finance and develop a legal and business environment supportive of timely payments in commercial transactions | 6. Access to finance for SMEs | Legal and regulatory framework |
| | | Source of external finance – bank financing |
| | | Source of external finance – non-banking financing |
| | | Venture capital ecosystem |
| | | Financial literacy |
| | | Digital financial services |
| 7. Help SMEs to benefit more from the opportunities offered by the EU's single market | 7. Standards and technical regulations | Overall co-ordination and general measures |
| | | Harmonisation with the EU acquis |
| | | SMEs access to standardisation |
| | | Digitalisation of standards and technical regulations |
| 8. Promote the upgrading of skills in SMEs and all forms of innovation | 8a. SME skills | SME skills |
| | 8b. Innovation policy | Policy framework for SME innovation |
| | | Government institutional support services for innovative SMEs |
| | | Government financial support for innovative SMEs |
| 9. Enable SMEs to turn environmental challenges into opportunities | 9. SMEs in a green economy | Framework for green and environmental policies targeting SMEs |
| | | Incentives and instruments |
| 10. Encourage and support SMEs to benefit from growth of markets | 10. Internationalisation of SMEs | Export promotion |
| | | Integration of SMEs into global value chains |
| | | OECD Trade Facilitation Indicators |
| | | SME use of e-commerce |

Source: (European Commission, 2008[2]).

To capture the growing importance of the digital economy, as well as all policy efforts made by EaP governments to support the digital transformation of SMEs, this report complements the SBA assessment with an analysis of selected framework conditions for the digital transformation (see the "Digital Economy for SMEs" chapter)[2]. The pillar on selected framework conditions for the digital transformation delves into i) the existence of a National Digital Strategy and its provisions for SMEs; ii) incentives and policies for increasing broadband connectivity; and iii) the promotion of digital skills across the population.

### Table 1.3. Assessment framework for the pillar on selected framework conditions for the digital transformation

| Components | Elements of analysis |
|---|---|
| National Digital Strategy | Existence of national digital strategies or equivalent documents<br>SME consideration within the policy document<br>Co-ordination mechanisms between stakeholders |
| Broadband connectivity | Investment in high-speed broadband infrastructures<br>Incentives for households, businesses and broadband providers<br>5G provisions<br>Data collection and assessment of digital divides |
| Digital skills | Policy documents for digital skills development<br>Involvement and co-ordination of relevant stakeholders<br>Inclusion of digital competence in school curricula<br>Lifelong learning initiatives<br>Data availability and monitoring |

This report is divided into two parts. Part I provides a comprehensive presentation of the assessment results categorised by thematic areas, with each chapter being dedicated to one thematic pillar. Part II presents individual country chapters, delving deeper into the assessment outcomes for each EaP country.

While this report is organised around the 12 SBA assessment dimensions, it is important to recognise that these dimensions are not stand-alone elements, as they interact with and complement one another in many ways. For instance, the *Access to finance* dimension is inherently interconnected to many of the other dimensions, as it serves as the fundamental prerequisite for SME development. Easy access to finance equips SMEs with the necessary resources to invest in *Entrepreneurial learning* and *SME skills*, as well as *Innovation* and access to *Business development services*. These inputs can enable enterprises to increase productivity and introduce innovation-oriented practices, which are crucial to their competitiveness and expansion into new markets through *Public procurement* and *Internationalisation* of their businesses. Nevertheless, access to new markets can be achieved only if businesses are given the opportunity to grow and thrive, which depends on a solid and effective *Institutional and regulatory framework* contributing to a well-functioning *Operational environment*.

The tight interconnection among all the pillars and dimensions underscores the necessity for policy makers to adopt a holistic perspective. Focusing on achieving results in a single dimension or area is therefore insufficient. Reform efforts in one area should be underpinned by progress and a solid foundation in all other dimensions, mutually working toward the success of SME support initiatives.

## The 2024 SBA assessment process

The SME Policy Index is based on the results of two parallel assessments. The five governments of the EaP countries conducted a self-assessment by completing a questionnaire and providing relevant evidence. In addition, the OECD and its partner organisations conducted an independent assessment that included inputs from a team of local experts, who collected data and information and conducted interviews with key stakeholders and private sector representatives[3].

The final scores are the result of the consolidation of these two assessments, enhanced by further research by the OECD and EBRD, as well as consultations with government and private sector representatives during country missions.

The 2024 SBA assessment was carried out between January 2022 and November 2023 in three phases:

- **Review of methodology and framework** (January 2022 – June 2022). The methodology and assessment framework were updated in consultation with all partner organisations, notably the European Commission, EBRD and ETF. SBA co-ordinators designated by EaP governments and relevant stakeholders in EaP countries were also consulted during three online stakeholders' meetings held between May and June 2022.
- **Data collection, verification and evaluation** (July 2022 – June 2023). During the data collection period, EaP countries carried out a self-evaluation of their policy frameworks via the assessment questionnaire. Kick-off country missions were held throughout September to November 2022 to provide an overview of the assessment process and timeline and offer a platform for an initial discussion of the main policy improvements since the previous assessment. Upon the receipt of countries' self-assessments, the OECD and EBRD conducted an independent assessment via extensive desk research and follow-up with relevant stakeholders in order to fill information gaps and resolve inconsistencies in findings. The assessment also benefitted from inputs by a team of local experts. In-country reconciliation meetings were held from March to May 2023 to discuss and verify the SBA assessment findings by presenting them to key SME policy stakeholders, including representatives of ministries and government agencies, international donors, civil society, academia, NGOs and business associations. On these occasions, focus group meetings with private sector representatives were conducted to gather further information.
- **Drafting, review and publication** (May 2023 – November 2023). The OECD and EBRD drafted country chapters that were sent to countries in June 2023, in advance of a regional SBA

stakeholders' meeting held in Paris on 19 June 2023, to share and discuss initial findings of the SBA assessment by thematic pillar and present countries' preliminary scores. Following discussions and comments provided during the regional SBA stakeholders' meeting and in bilateral consultations over the following months, both country profiles and thematic chapters were updated. The draft report – *SME Policy Index: Eastern Partner Countries 2024* – was then reviewed extensively by OECD staff and partner organisations, before being officially launched at OECD Eurasia Week in December 2023. The publication will also be launched in the five EaP countries with dedicated dissemination events in the first half of 2024.

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OECD (2022), *Recommendation of the Council on SME and Entrepreneurship Policy*, https://legalinstruments.oecd.org/en/instruments/OECD-LEGAL-0473. [1]


## Notes

[1] Following Belarus's involvement in Russia's war of aggression against Ukraine, co-operation with Belarus has been suspended. Therefore, the 2024 assessment does not cover Belarus and any mention of the Eastern Partner countries throughout the report refers exclusively to Armenia, Azerbaijan, Georgia, the Republic of Moldova, and Ukraine.

[2] For more information on the relevance of digitalisation for SMEs in EaP countries and on the rationale for broadening the assessment by covering this topic, please refer to the chapters on "Economic context" "Digital Economy for SMEs" and to Annex A, "Methodology for the Small Business Act assessment".

[3] A cut-off date of 30 June 2023 was established for the assessment. Only policy developments and reforms implemented by that date were taken into account for the calculation of the SME Policy Index scores. Reforms and policy developments that have taken place after that date (by September 2023) are reflected in the text.

# 2 Overview: 2024 SME Policy Index scores and key findings

## Overview of 2024 key findings for Eastern Partner countries

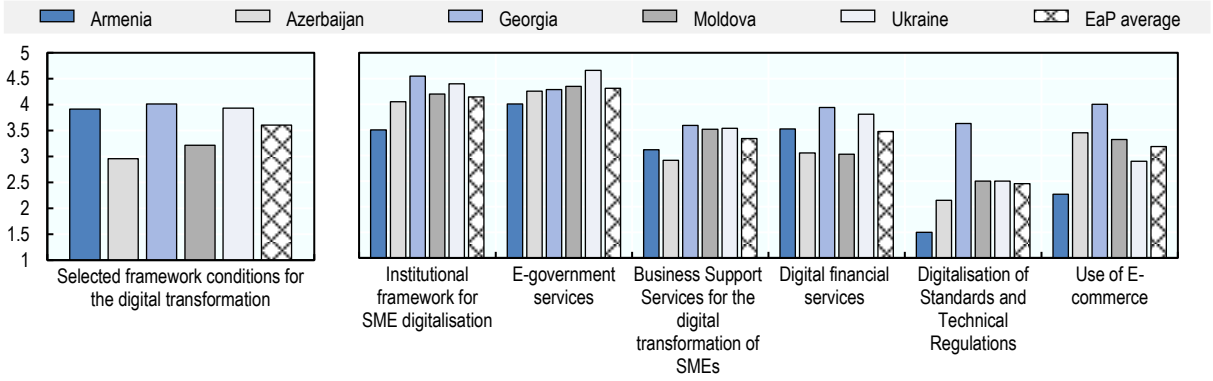
This section provides an overview of key findings of the 2024 Small Business Act for Europe (SBA) assessment for all Eastern Partner (EaP) countries across the dimensions of the five thematic pillars and the selected framework conditions for the digital transformation, as well as key findings for each country. A detailed analysis and cross-country comparison of each pillar and dimension is presented in Part I of this report, while Part II contains full country profiles. Complete scores per dimension, sub-dimension, and thematic block found in Table 2.22 at the end of this chapter. The scoring methodology is presented in Annex A.

### *Key findings by pillar*

#### *Digital Economy for SMEs*

Because of the increasing and strategic importance of the topic, this new round of the SBA assessment entails a new section dedicated to the digital transformation. A pillar on selected framework conditions for the digital transformation has been added, assessing national digital strategies and measures for broadband connectivity and digital skills, while pre-existing pillars contain digitalisation-oriented sub-dimensions. The OECD calculated a weighted average of the scores for each of these aspects, resulting in overall composite scores for SME digitalisation policies (Figure 2.1).

**Figure 2.1. Composite scores for SME digitalisation policies in EaP countries, by component**




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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## Table 2.1. Performance in selected framework conditions for the digital transformation

| Selected framework conditions for the digital transformation | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| 2024 scores | **3.92** | **2.96** | **4.02** | **3.22** | **3.93** | **3.61** |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

The section below summarises the main findings of the assessment of selected framework conditions for the digital transformation, examining i) the overall policy framework for the digital transformation, including the national digital strategy or its equivalent; ii) broadband connectivity; and iii) digital skills.

### National Digital Strategy

National digital strategies allow governments to outline their approaches to a topic by listing their policy priorities and objectives in this regard. These strategies can help countries accelerate the digital transformation of their economies and societies by ensuring a comprehensive policy approach and facilitating co-ordination among various stakeholders (Gierten and Lesher, 2022[1]).

EaP countries have prioritised the integration of digitalisation into their policies and have been developing policy frameworks to achieve this, although these differ in nature and scope. Among them, Armenia stands as the only country in the region to have already adopted a National Digital Strategy (NDS), the *Digitalisation Strategy of Armenia for 2021-25*. Meanwhile, Azerbaijan, Georgia and Moldova have formulated similar multi-year strategies, but these are awaiting approval and are expected to be adopted by the end of 2023. Policy objectives related to digitalisation are currently dispersed across different policy documents, including overarching country strategies like in Azerbaijan and Georgia, or an innovation strategy for Moldova. Georgia has also incorporated digitalisation-related provisions in its ongoing broadband and SME strategies. Finally, Ukraine has embedded its strategic vision for digital transformation in several governmental documents[1], including the *National Economic Strategy 2030*.

However, the current policy documents for the digital transformation allocate limited attention to the digitalisation of SMEs in non-IT sectors. Armenia's NDS includes provisions to expedite SME digitalisation, particularly by raising the private sector's awareness about digital tools, promoting businesses' use of new technologies, and further advancing e-commerce and innovative solutions. Other EaP countries have outlined a few measures in these strategies, yet these remain limited and often revolve around digital skills.

Regarding policy governance, all EaP countries have put forth efforts to establish multi-stakeholder approaches. The formulation of strategic policy documents for digitalisation has benefitted from contributions from various actors. Typically, this involves the establishment of dedicated working groups comprised of ministries, public agencies, international experts (consulting firms and/or international organisations), and sometimes businesses and business associations. These mechanisms, along with the clear designation of leading stakeholders for the NDS, have facilitated co-ordination among these actors.

One of the main weaknesses for most EaP countries remains the deficiency in data collection related to digital transformation, which impedes monitoring and evaluation practices. Besides insights on broadband connectivity, statistical offices only collect a limited number of indicators, and this rarely covers businesses' adoption and use of digital tools. In this context, Georgia and Ukraine appear as frontrunners and Azerbaijan has recently made substantial progress. Nonetheless, more could be done to align with OECD and EU databases and methodologies. Current policy documents lack quantifiable targets to assess progress, such as advancements in digital skills development and SME digitalisation.

EaP countries could strengthen their policy frameworks for the digital transformation by:

- **Consolidating policy approaches to digitalisation and ensuring co-ordination throughout implementation**: EaP countries should adopt comprehensive NDSs that outline clear objectives, measurable targets, and budgets. Successful implementation will require the involvement and co-ordination of all relevant public and private stakeholders.
- **Promoting inclusive SME digitalisation**: Policymakers must include provisions for digitalisation in small non-IT businesses, fostering both technology adoption and digital culture.
- **Ensuring effective monitoring and evaluation**: Countries should collect more data on the digital transformation to foster evidence-based policymaking and efficient impact evaluation.

### Broadband connectivity

A crucial prerequisite for economies and societies to harness the potential of digital transformation lies in securing Internet access that is efficient, affordable and dependable. Not only do some OECD countries acknowledge this as a fundamental right, but it is also listed as one of the United Nations Sustainable Development Goals (SDGs).

Over the past years, broadband adoption has been steadily increasing in EaP countries, although significant disparities remain. Georgia stands out as the most connected EaP country, while Ukraine has demonstrated significant progress, witnessing a remarkable increase of 52% in fixed subscriptions and 254% in active mobile subscriptions between 2016 and 2021. However, despite this advancement, connectivity levels in the EaP region still fall short of the benchmarks set by both the OECD and the EU.

The quality of broadband is another critical factor for enabling individuals and businesses across the EaP region to fully benefit from digitalisation. However, recent data underscores persisting regional disparities. For example, while Moldova and Ukraine benefit from a good connection speed – one that is comparable to OECD and EU levels – Azerbaijan grapples with Internet speed challenges.

Moreover, affordability remains a concern. Although ICT prices are among the cheapest in the world in absolute terms, a comparison of tariffs as a percentage of gross national income (GNI) per capita reveals that Internet access remains relatively less affordable in the EaP region than in OECD and EU countries, particularly for fixed broadband. In 2021, Armenia, Georgia and Moldova still exceeded the ITU's 2% threshold.[2] This affordability challenge can hinder business uptake, especially in conducting online operations that require robust, fast and dependable connections, a demand which fixed broadband is better suited to meet.

Data remains scarce across EaP countries regarding broadband uptake among businesses. Only Georgia and Ukraine have collected such indicators, revealing that firms' connectivity in their territories lags behind that of OECD and EU countries. The gap in connectivity between SMEs and large enterprises is also more pronounced: For instance, in Ukraine, 84.5% of small firms have access to the Internet compared to 96% in the OECD. Similarly, most small Georgian companies do not have access to high-speed Internet (Geostat, 2022[2]).

Policymakers across the EaP region have been taking measures to tackle these digital divides. Georgia has prioritised the development of high-speed Internet by formulating a dedicated broadband strategy aimed at increasing competitive pressure, attracting investments, and building digital skills and demand. Armenia and Ukraine have been developing their broadband plans, although they are yet to be finalised and adopted. Current national broadband policies in EaP countries prioritise the expansion of fibre and/or 5G technology and investment in infrastructure development. However, broadband policies could benefit from more regular consultations with relevant stakeholders. A sustained multi-stakeholder dialogue involving consumers, network operators, local governments and regulatory could help ensure that the opinions of all parties are adequately considered (OECD, 2021[3]).

Moving forward, key recommendations for policymakers include:

- **Fostering competition,** e.g. by promoting co-investment, infrastructure sharing, and adequate legal and regulatory frameworks. The latter should undergo regular reviews to ensure their continued adequacy. Making multistakeholder consultations on Internet connectivity a more integral part of policy formulation is highly important in this regard.
- **Increase demand for quality broadband** by fostering digital literacy among citizens and firms, addressing information asymmetries and providing open and reliable data on subscriptions, coverage and quality of service.

#### Digital skills

Digital skills are an absolute pre-requisite for a successful digital transformation. Economies and societies indeed need both digital-savvy citizens to tap into the potential of new technologies in everyday life, and IT specialists to meet increasing labour market demand.

All EaP countries have made good progress in including digital competence in their education curricula. Armenia and Moldova have included it as a key competence for all education levels, while Georgia has focused its formal education efforts on vocational education and training (VET). In most of them, teacher training in digital fields has also been on the rise. Lifelong learning opportunities in digital skills for citizens have widened, considerably fostered by private sector stakeholders across the region. On the other hand, support for digital skills development among small firms remains limited. In general, Ukraine appears at the forefront of digital literacy measures: the country has implemented a wide range of initiatives and tools, including a self-assessment test for individuals to evaluate their digital skills and a digital competence framework based on the EU's Digital Competence Framework for Citizens (DigComp) to serve as a common reference.

Nevertheless, digital skills levels across the region have not yet reached OECD and EU levels. Data collection on digital literacy remains an important issue, with few insights being available, especially on firms. While EaP countries have included digital skills provisions in overall policy initiatives for digitalisation, the lack of available indicators impedes monitoring and evaluation. Skills assessment and anticipation exercises are also still at a nascent stage in all EaP countries, with only Georgia having developed a systemic approach. Indeed, most tools, such as surveys and/or sectoral studies, are conducted on an ad hoc basis by donors/development partners. Labour market forecasts, when available, do not delve into digital skills aspects.

Finally, while several ministries and governmental agencies are involved in the elaboration of digital skills policies, the latter could benefit from a stronger involvement of certain stakeholders – such as ministries of labour and national employment agencies, but also teachers and private sector representatives.

Going forward, policymakers could complement their existing policy approaches by:

- **Strengthening multi-stakeholder approaches to digital skills development**
- **Implementing digital skills as a key competence at all education levels**
- **Adopting a framework for digital competences to serve as a common reference**, following the example of DigComp 2.1
- **Developing digital skills assessment and anticipation tools**
- **Stepping up support for digital skills development among firms, especially small ones.**

### *Pillar A: Responsive Government*

To adeptly navigate the intricate interplay between SME policy and other domains of policymaking, governments must establish a clear vision for SME policy that is backed by strategic guidelines. They must foster a broad consensus amongst all stakeholders, including the business community, SME associations, non-governmental organisations (NGOs), and relevant partner organisations. Pillar A, which iscentred on

responsive government, assesses the progress achieved by EaP countries since 2020 regarding the institutional and regulatory framework for SME policy, the operational environment for SMEs, and bankruptcy and second chance.

### Institutional and regulatory framework for SME policy

Creating robust and transparent institutional and regulatory framework is pivotal in promoting entrepreneurship and bolstering SME growth. This includes defining clear parameters to identify SMEs; identifying institutions responsible for SME policy design, delivery, monitoring and evaluation; and devising mechanisms for policy discussion and alignment.

The EaP region has made incremental progress in this dimension since 2020 (see Table 2.2). All the countries, except for Armenia and Ukraine, reported gradual improvements across most of the sub-dimensions, with Georgia confirming its position as a frontrunner. These results demonstrate the region's commitment to SME support and business environment reforms during a particularly challenging period, characterised by a series of negative events that have disrupted policymaking, including the COVID-19 pandemic and Russia's full-scale invasion of Ukraine. Nevertheless, all the countries have aligned their national SME definitions with that of the EU in terms of employment criteria, though other parameters still differ. Almost all EaP governments have developed medium-term SME strategies, with variations in structure and evaluation practices.

However, sectoral gaps persist. By the end of June 2023, Georgia was the only country implementing a dedicated strategy covering the period 2021-2025. SME development agencies have expanded beyond entrepreneurship promotion to offer targeted business services supporting enterprise growth and digitalisation; and in Armenia, Georgia and Moldova they also provide credit guarantees to SMEs. Azerbaijan, Georgia, Moldova and Ukraine enhanced their agencies' capacities during the pandemic. Nevertheless, legislative and regulatory simplification, including RIAs, witnessed a setback due to pandemic-related disruptions.

Some progress has been made. Moldova stands out as a leader in systematic RIA application. EaP governments have made strides regarding public-private consultations, reflecting improved online practices and greater SME involvement. Finally, all countries have started taking SME digitalisation into consideration in their institutional and policy frameworks for SMEs, with the establishment of electronic platforms, strategic directions, agency roles, and monitoring across the region. In fact, Armenia, Azerbaijan, Georgia and Ukraine have displayed a strong commitment to SME digital transformation, having allocated resources to relevant agencies.

Looking forward, policymakers should focus on:

- Securing implementation through shorter-term action plans and creating synergies between SME development strategies and sector/activity-oriented development plans.
- Developing more advanced instruments of policy co-ordination with other sets of strategies (local development, skill development and digitalisation) and the broader national economic development plans.
- Systematically applying RIA to all new legislative and regulatory acts that are expected to have a significant impact on the business sector and introducing RIA SME tests.
- Upgrading the governance mechanisms of SME agencies, following the recent example of Moldova.
- Broaden the involvement in public private consultation (PPC) including by expanding the use of digital platforms and involving businesses operating in new emerging sectors (i.e., ICT, agri-bio enterprises, small tourist operators and logistics).

- Strengthen policy and institutional frameworks for the digital transformation of SMEs in non-IT sectors.

### Table 2.2. Progress in the institutional and regulatory framework dimension

| Institutional and regulatory framework | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| 2024 scores | **3.24** | **3.69** | **4.37** | **3.93** | **3.68** | **3.78** |
| *2024 scores (CM)* | *3.29* | *3.49* | *4.19* | *3.82* | *3.80* | *3.72* |
| *2020 scores (CM)* | *3.68* | *3.36* | *3.69* | *3.68* | *3.64* | *3.61* |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### Operational environment for SMEs

The *operational environment* for SMEs is essential for fostering business growth without undue bureaucratic barriers. This dimension evaluates the extent to which public administrations have undertaken efforts to simplify regulations, reduce costs and alleviate administrative burdens on SMEs.

Since 2020, the operational environment for SMEs in the EaP region has improved overall. All EaP countries have made significant progress by increasing their provision of e-government services. Ukraine's Diia initiative is seen as the most advanced tool in this regard, providing a wide range of e-services accessible throughout the country. Digital government platforms are also operational in Armenia, Georgia, and Moldova.

However, data collection on SME e-government services usage remains limited. All EaP countries offer company registration procedures that are relatively simple, fast and inexpensive; Georgia and Armenia have confirmed their position as leaders in this area. Business licensing has also advanced, as all EaP countries have streamlined procedures and established online portals to handle applications. Moldova's one-stop-shop platform and Georgia's provision of online services serve as good examples on this matter. Tax compliance procedures have evolved, most notably because the COVID-19 pandemic prompted temporary tax measures for economic recovery. In fact, since 2020, EaP countries have introduced simplified tax regimes, and efforts to ease tax declaration and payment procedures have continued.

EaP countries should maintain this momentum in policymaking by focusing on the following:

- Collecting data on the use of e-government services by different categories of SME (by size, type of ownership and location) to improve their design.
- Regularly gathering indicators on online registration and monitor the performance of registration agencies across the countries.
- Calculating the effective tax rate applied to different categories of SMEs and evaluating the impact of special tax regimes and tax incentives on individual entrepreneurs and small enterprises to avoid distorting effects.
- Implementing an automatic VAT-refund system and minimising the potential for fraud and misuse by applying risk-assessment technics.

## Table 2.3. Progress in the operational environment dimension

| Operational environment framework | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| 2024 scores | **3.99** | **4.25** | **4.51** | **4.34** | **4.11** | **4.24** |
| *2024 scores (CM)* | 4.05 | 4.28 | 4.65 | 4.50 | 4.36 | 4.37 |
| *2020 scores (CM)* | 2.92 | 4.44 | 4.33 | 3.48 | 3.70 | 3.77 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### Bankruptcy and second chance

Efficient insolvency regimes are essential for ensuring a healthy market since well-structured laws enhance capital allocation, increase productivity and boost cross-border investment. More specifically, timely detection of financial distress, early warning mechanisms, advisory services, well-designed bankruptcy procedures, and second-chance initiatives are crucial in supporting SMEs. This dimension assesses the extent to which EaP countries are facilitating market exit and re-entry by adopting effective and efficient frameworks to prevent and face insolvency, as well as to re-start a business after bankruptcy.

The EaP region's progress in the areas of bankruptcy and second chance has been uneven. All countries, except Armenia, have demonstrated some improvement since the 2020 assessment. However, overall, this dimension remains one of the weakest performance areas, explained by insufficient preventive measures and second chance promotion initiatives. All EaP countries show significant room for improvement in their measures to identify financial distress and prevent insolvency. While in all the countries (except Armenia) businesses in financial distress can access information on available government support, information on tools and support for SMEs often lacks visibility and accessibility. Moreover, all the countries except Georgia have yet to develop systems to monitor existing measures to prevent insolvency.

Regarding survival procedures, EaP countries prove to have well-designed bankruptcy frameworks. However, average scores were negatively affected by changes to the assessment methodology. Somewhat positive results emerged from the EBRD Business Reorganisation Assessment, which showed that, on average, EaP countries perform at the same level as other assessed countries. In addition, since 2020, all countries except Ukraine have amended their legislative framework for bankruptcy, bringing important improvements. However, more comprehensive data collection and monitoring efforts are needed. Promoting second chance appears as the weakest sub-dimension since none of the EaP countries have comprehensive policies or strategies promoting a fresh start for entrepreneurs' post-bankruptcy.

Moving forward, EaP countries should:

- Establish comprehensive early-warning systems to prevent bankruptcy.
- Introduce simplified insolvency proceedings for small cases or SMEs.
- Adopt proactive second-chance strategies, facilitating fresh starts for honest entrepreneurs.
- Develop monitoring mechanisms for insolvency procedures and programmes.
- Collect systematic data on SME insolvency for informed policies.

### Table 2.4. Progress in the bankruptcy and second chance dimension

| Bankruptcy and second chance | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| 2024 scores | **1.97** | **1.91** | **3.36** | **2.00** | **2.52** | **2.35** |
| *2024 scores (CM)* | 2.35 | 3.10 | 3.49 | 2.79 | 3.75 | 3.10 |
| *2020 scores (CM)* | 2.66 | 2.76 | 3.06 | 2.63 | 3.24 | 2.87 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## *Pillar B: Entrepreneurial Human Capital*

Entrepreneurial human capital is essential for economic growth, competitiveness, job creation and wellbeing. This pillar assesses the policy design, implementation and monitoring of the policies in the following areas, which are key for human capital development:

- *Entrepreneurial learning* – development of entrepreneurship key competence as a combination of knowledge, skills and attitudes people should possess for successful career and personal development;
- *Women's entrepreneurship* – the creation of a policy environment in which women can engage on equal terms with men in entrepreneurship, the creation of new jobs, and generation of new value for the national economies and internationally; and
- *Skills for SMEs* – the development of specific, occupational skills for successful entrepreneurship.

### Entrepreneurial learning and women's entrepreneurship

*Entrepreneurial learning*, which is a central theme of Principle 1 of the SBA, fosters essential competencies and mindsets for economic growth. It transforms societal views, driving innovative human capital.

Since 2020, EaP countries have worked to advance policies and develop frameworks supporting entrepreneurial learning. The EaP average score for this dimension is 3.64, with Georgia and Moldova leading the way. Ukraine has integrated entrepreneurial learning into its overarching economic strategy, while most countries have incorporated it into their education strategies and, in the case of Armenia and Georgia, into their SME strategies. However, not all countries have established formal policy partnerships on entrepreneurial learning.

Significant progress has been made in embedding entrepreneurship as a key competence in national curricula. Armenia and Azerbaijan have made notable strides by updating their curricula to highlight entrepreneurial mindset and skills, with the latter launching new VET infrastructure and career guidance services. Georgia has made efforts to align with the Entrepreneurship Competence (EntreComp) Framework. Online learning solutions, catalysed by the COVID-19 pandemic, have paved the way for the development of innovative teaching methods. Azerbaijan's *tehsilim.edu.az* and Ukraine's All-Ukrainian Online School are good examples of the creation of dedicated online platforms. There has been additional progress on teacher training across most countries, with major progress being achieved in Georgia with the establishment of a Skills Agency.

In addition, EaP countries have been making efforts towards developing non-formal learning opportunities on entrepreneurship. Azerbaijan, Moldova and Ukraine have introduced normative-legal frameworks to allow for the certification of competencies acquired in informal ways.

Finally, collaboration between higher education institutions and businesses has been growing across the region, often with donor support, promoting innovative practices. However, co-operation between general schools and SMEs on entrepreneurial learning remains underdeveloped.

Overall, while strong achievements have been shown, the monitoring and evaluation of policies – including learning outcomes, teacher competencies, and students' labour market results – need to be enhanced to ensure policy impact.

*Women's Entrepreneurship*

This dimension is embedded within Principle 1 of the SBA, which addresses gender disparities in business ownership. It highlights the need for comprehensive policies, collaborative approaches and disaggregated data to bridge gender gaps and empower women's engagement in business.

EaP countries have sustained efforts to support women entrepreneurs. Georgia and Moldova maintain strong performances across all thematic blocks, averaging 4.90 and 4.40, respectively, while Ukraine has made impressive progress, reaching 4.21. Armenia's approach remains consistent, addressing the topic in policy documents. All the countries have implemented a range of support measures for women entrepreneurs, albeit to a varying extent. Most of these initiatives are promoted online, primarily through the official websites of SME agencies and/or business associations at the national level. Ukraine stands out as the only country to have created a comprehensive one-stop-shop, Diia.Business, offering a consolidated view of the available support measures. In addition, territorial coverage has broadened, with the establishment of several regional initiatives and/or support centres to assist women entrepreneurs. Efforts to bridge the gender gap in STEM fields have progressed, focusing on awareness-raising and IT skills training. Private sector involvement and international donor support continue to bolster women's entrepreneurship initiatives. However, formal policy partnerships and comprehensive action plans are lacking, notably in Azerbaijan.

While data on women's entrepreneurship remains limited, available insights do shed light on persisting challenges, despite notable improvements. Barriers include access to finance and networks, as well as gender stereotypes, which were exacerbated by the COVID-19 pandemic, as the containment measures increased time spent on domestic tasks. Addressing these issues requires better data. While there are studies assessing barriers to women's entrepreneurship in these countries, apart from Ukraine, these are not conducted annually.

EaP countries have made noteworthy progress in entrepreneurial learning and women's entrepreneurship. Nevertheless, to advance, EaP countries should consider:

- Strengthening policy frameworks for entrepreneurial learning, including introducing entrepreneurship as a key competence at all education levels.
- Stepping up efforts on teacher training.
- Enhancing co-operation between schools and SMEs to offer practical experiences for students.
- Improving monitoring and evaluation practices for entrepreneurial learning outcomes.
- Ensuring co-ordination among stakeholders involved in women's entrepreneurship policies and programmes.
- Collecting more comprehensive data on gender-related issues and assessing the impact of existing programmes.
- Extending support measures beyond early-stage entrepreneurship to aid women entrepreneurs in scaling up.
- Addressing gender stereotypes and promoting women's participation in higher value-added sectors.
- Developing incentives to reduce women's participation in the informal economy.

## Table 2.5. Progress in the *Entrepreneurial learning* and *Women's entrepreneurship* dimensions

| Entrepreneurial learning and women's entrepreneurship | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **2.91** | **3.07** | **4.17** | **4.09** | **3.95** | **3.64** |
| *2024 scores (CM)* | 3.35 | 3.70 | 4.74 | 4.74 | 4.56 | 4.22 |
| *2020 scores (CM)* | 2.60 | 3.89 | 4.45 | 4.29 | 3.83 | 3.81 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### SME skills

Principle 8 of the SBA emphasises the significance of enterprise skills in unlocking SMEs' potential and fostering national economic growth. This SME skills dimension is focused on two main themes, namely the provision of training services for SMEs and skills intelligence and its use for policy and practice.

All EaP countries have made progress in this area since the previous assessment. Notable advancements were observed in Moldova and Ukraine, which have been catching up with Georgia, while institutional changes disrupted improvements in Armenia. SME training services have been made available in all EaP countries and opportunities continue to be expanded. Azerbaijan and Ukraine have made noteworthy progress in this regard with the creation of a network of operators by KOBIA in the former and the launch of Diia.Business for entrepreneurial knowledge and consulting in the latter. All the countries have made efforts to develop courses covering different skills, notably digital and green ones. Moldova is a leader in this domain, with its SME Agency, ODA, having implemented several full-fledged programmes. Georgia has been actively working towards expanding its support, notably for the digital transformation of small firms in non-IT sectors. Meanwhile, Armenia's approach differs, with most of its SME/start-up skills development programmes being delivered by NGOs.

Online training has also become increasingly available in EaP countries. However, its implementation across the region is uneven. Moreover, the learning outcomes and overall impact of the materials launched thus far could be made more interactive. Georgia, Moldova and Ukraine are enhancing smart specialisation strategies for growth, but further measures such as targeted training are needed to fully engage SMEs in prioritised areas.

On SME skills intelligence, most EaP countries have enhanced their frameworks, gathering sex-disaggregated training statistics and feedback helping to inform new course development. However, assessing the tangible impact of training on skills and SME performance remains infrequent. National frameworks for SME skill data collection and analysis have been strengthened, with Georgia leading through annual surveys and sector-specific studies, and Azerbaijan making notable progress since 2020. Armenia and Ukraine have yet to fully implement such practices.

Finally, skills assessment and anticipation tools in the EaP region are early in their development.

Moving forward, EaP countries could strengthen their approaches to SME skills development by:

- Raising awareness of available training provisions for SMEs.
- Developing online training opportunities by introducing innovative and digital learning methods.
- Capturing the impact of training on skills development and SME performance to improve monitoring and evaluation practices.
- Introducing certification of the skills acquired, to help ensure the quality of training.

- Strengthening systemic approaches to data collection on SME skills, training, and barriers to participation in training.
- Implementing skills anticipation tools.
- Offering courses to SMEs in the priority areas identified for smart specialisation.

### Table 2.6. Progress in the SME skills dimension

| SME skills | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **2.37** | **3.59** | **4.12** | **3.89** | **3.91** | **3.57** |
| *2024 scores (CM)* | 2.13 | 3.80 | 4.43 | 4.40 | 4.12 | 3.78 |
| *2020 scores (CM)* | 1.80 | 2.80 | 4.00 | 3.30 | 2.97 | 2.97 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## *Pillar C: Access to Finance*

Access to finance can be regarded as the prime accelerator for an SME's economic growth. However, it remains, in the EaP region as elsewhere, a challenge for SMEs. In EaP countries, the financing gap is estimated to be about USD 44 billion (18% of the countries' GDP), meaning that, for SMEs' needs to be fully met, current lending amounts would need to increase by 200%.

This pillar covers six dimensions linked to access to finance: (i) the legal and regulatory framework for bank financing, (ii) the provision of bank financing, (iii) the conditions for non-bank financing, (iv) the ecosystem for venture capital, (v) financial literacy and (vi) digital financial services. The last dimension constitutes an innovation with respect to previous assessments.

### Access to finance

Since 2020, many governments have put in place new or larger support mechanisms for access to finance, enacted legal reforms to simplify SMEs' use of non-bank financing solutions, and conducted more regular assessments on financial literacy. All economies in the region have a reasonably developed legal framework for secured transactions in place, but effective enforcement remains a challenge. Cadastres exist in all countries and are available online and to all stakeholders, and there has been no major change in that regard since the last assessment. Registers for movable assets are also in place across the region and all financial institutions can access them. In Ukraine, online access was restricted after Russia's invasion and access must be specifically requested. All central banks in the region have a credit register, and private credit bureaus have been further developing. In terms of coverage, most credit bureaus go beyond collecting information from financial institutions, but sources of credit information could be expanded further in some countries, e.g. Moldova and Ukraine. Countries have made progress with the implementation of Basel III requirements – Moldova has now followed Georgia's lead in fully implementing all requirements, while Armenia, Azerbaijan and Ukraine have made progress on implementation, although Ukraine relaxed some prudential requirements after Russia's invasion. Loan dollarisation levels remain high in all EaP economies. All central banks, except Ukraine's, have enacted certain conditionalities to encourage local currency lending, e.g. higher risk weights and mandatory disclosure of foreign exchange risk to borrowers.

The inclusion of ESG indicators in banks' reporting obligations is not yet widespread. The National Bank of Georgia is the only financial authority in the region that has already developed a green taxonomy to simplify green financing instruments' charting, and banks need to systematically report on these aspects. With regard to capital markets, none of them in the region are sufficiently developed to be seen as a realistic funding option as local stock exchanges suffer from all-too-limited investor bases.

All economies in the EaP region have implemented credit guarantee schemes. These programmes are increasingly supplemented by consultancy and advisory services for business development. Strengthening private participation in the schemes could bring benefits, especially in Armenia and Azerbaijan. Except for Georgia, none of the schemes are subject to proper impact evaluations.

While microfinance is widely available across the EaP region, leasing and factoring are still underused compared to countries of similar size, notably due to inadequate legal frameworks and lack of entrepreneurs' awareness and available data. Ukraine still does not have a dedicated legal framework for microfinance. Venture capital is at an early stage and the lack of funding beyond the seed stage constitutes a serious drawback for start-ups.

All countries in the region conduct financial literacy assessments, usually led by national oversight bodies, and in some cases supported by international donors (e.g. Ukraine). There has also been notable progress on digital financial services among a few outsiders (Armenia, Georgia and Ukraine). All EaP countries monitor data protection and sharing, and all authorities, except for Armenia's, require institutions to share data amidst certain circumstances. An operational resilience framework for financial service providers is also in place everywhere, but only Armenia, Georgia and Moldova regulate outsourcing in the financial services sector. Nevertheless, none of the countries in the region have implemented a multi-stakeholder approach to digital finance supervision so far.

### Table 2.7. Progress in the *Access to finance* dimension

| **Access to finance** | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **3.54** | **3.31** | **4.07** | **3.48** | **3.40** | **3.56** |
| *2024 scores (CM)* | 3.87 | 3.74 | 4.30 | 3.94 | 3.63 | 3.90 |
| *2020 scores (CM)* | 3.86 | 3.32 | 3.85 | 3.78 | 3.54 | 3.67 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Moving forward, EaP countries could:

- Improve enforcement frameworks for secured transactions.
- Ensure adequate monitoring and evaluation mechanisms for financial support programmes, by going beyond the collection of basic usage data.
- Improve availability and collection of statistics in the financial sector, by displaying an inclusive approach towards non-bank financing sources.
- Establish support mechanisms for developing growth-stage funding for start-ups, e.g. via government participation in specific venture capital (VC) funds, or the establishment of a fund of funds.
- Develop strategic directions for digital financial service regulation and regularly consult both public and private stakeholders.

#### *Pillar D: Access to Markets*

SMEs in the EaP region have substantial opportunities in international markets and public procurement. Involvement in public procurement not only drives business growth but also promotes competition, enhances value for money and fosters innovative solutions. Similarly, global trade offers chances to join value chains and enhance innovation and productivity. However, SMEs face challenges accessing these markets due to information gaps, incompatible quality standards, complex procedures and limited resources. Targeted policies are essential to overcome these barriers and expand market opportunities.

This pillar assesses EaP reforms in public procurement, standards and technical regulations, and SME internationalisation.

### Public procurement

SME involvement in public procurement offers mutual benefits to both businesses and the public. Such participation is crucial for economic recovery, acting as a shield during crises. However, challenges such as complex procedures, resource constraints, and stringent qualification requirements hinder SMEs' entry into the markets. This dimension evaluates EaP countries' efforts to foster a more inclusive public procurement market for SMEs.

The results of the SBA assessment in public procurement indicate a noticeable change in the trajectory of EaP countries' performance. While some countries show progress in policy implementation and monitoring of public procurement (Azerbaijan, Moldova and Ukraine), all countries exhibit a deterioration of the regulatory framework.

Standard public procurement procedures have been put aside in favour of less competitive alternatives to face urgent needs resulting from the COVID-19 pandemic and the war in Ukraine, which have also brought delays in approval and implementation of strategic initiatives. Since 2020, public procurement laws have only been slightly amended and medium-term strategic frameworks have seen limited progress, while harmonisation between public procurement strategies and strategies in related fields is lacking. Institutions in charge of public procurement are affected by capacity and skills gaps and conflicts in decision-making roles. E-procurement systems exist but are underutilised, although some progress has been made in the provision of public access to data on procurement activities.

**Table 2.8. Progress in the public procurement dimension**

| Public procurement | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **2.80** | **2.55** | **3.61** | **3.16** | **3.61** | **3.15** |
| *2024 scores (CM)* | 2.92 | 2.70 | 3.44 | 3.35 | 3.25 | 3.13 |
| *2020 scores (CM)* | 3.83 | 2.66 | 4.26 | 3.98 | 3.22 | 3.59 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Going further, policymakers should:

- Expand and improve regulations facilitating SME participation in public procurement.
- Strengthen the capacity of central institutions by providing training, reviewing complaints, and implementing a monitoring system.
- Ameliorate the sequencing of e-procurement and exploit it for generating and using data.
- Encourage SME participation by leveraging centralised purchasing and framework agreements and providing training to improve SMEs' trust and participation.
- Raise the status of procurement officers and improve their knowledge and skills, in order to avoid corruption.

### Standards and technical regulations

Technical regulations establish essential criteria for products before their market introduction, while standards promote interoperability and fair competition, thereby fostering innovation and trade. SMEs,

often challenged by foreign standards and costly procedures, need accessible information and support for compliance. This dimension examines quality infrastructure alignment.

All EaP countries have made progress regarding standards and technical regulations, with the EaP average score increasing from 3.67 in 2020 to 3.98 in 2024 using comparable methodology. Georgia remains the leader of this dimension, having reached a score of 4.37. Each country has a designated government body responsible for the overall co-ordination of technical regulations and quality infrastructure (QI). Georgia has established an independent Market Surveillance Agency (MSA), while Ukraine has progressed in its negotiations with the EU on Agreements on Conformity Assessment and Acceptance of Industrial Products (ACAA), and Moldova has aligned its legislation to bring technical regulation in line with the provisions of the World Trade Organization (WTO) Agreement on Technical Barriers to Trade (TBT).

All the EaP countries have adopted measures to ensure their technical regulations and standardisation laws harmonise with the EU *acquis*. Armenia, Georgia, Moldova and Ukraine have an action plan or a similar document on transposing EU sectoral legislation in priority sectors. Georgia's, Moldova's and Ukraine's standards bodies were granted a CEN and CENELEC Affiliate status, which was approved in 2022 and entered into force in January 2023. Except for Azerbaijan, the adoption rate of EU standards is at least 50% in priority sectors. All countries have accreditation bodies, although only those of Georgia and Moldova have been completely positively assessed by the European Co-operation for Accreditation (EA) or by peer organisations. Azerbaijan does not have legislation on conformity assessment in line with the *acquis*. Likewise, Armenia's legislation is not totally in line with the *acquis*, which also influences its specific conformity assessment activities. Conformity assessment bodies in line with EU requirements exist in Ukraine's priority sectors. Georgia and Moldova have such bodies in most priority sectors. All five countries have an operational metrology body, although only Armenia, Georgia and Ukraine also have a strategy for metrology. Most of the five countries have legislation on metrology in line with the *acquis*, while Azerbaijan is preparing a proposal for such legislation. Market surveillance is more advanced in Georgia and Ukraine, while Armenia, Azerbaijan and Moldova lag behind.

All countries have implemented measures for SME awareness and developed mentoring programmes. Concerning digitalisation, on average, countries demonstrate relatively low scores. Most of them offer support to SMEs for their integration into the EU Digital Single Market. Additionally, most have a strategy for the digitalisation of processes within the authorities responsible for technical regulation. However, there is room for improvement.

Moving forward, EaP countries could implement the following recommendations:

- Enhance market surveillance quality infrastructure and intensify its understanding.
- Seek international recognition for quality infrastructure.
- Develop standards education strategies with SME-specific considerations.
- Establish financial measures to further support SME participation in standardisation.
- Improve the digital maturity of the technical regulation system and quality infrastructure, particularly in conformity assessment.
- Create export platforms tailored for SMEs trading with the EU where absent.
- Improve the regular evaluation of the technical regulation system and quality infrastructure, considering areas *with* and *without* regular assessment.
- Continue with good practice from Twinning projects after their completion.

### Table 2.9. Progress in the standards and regulations dimension

| Standards and regulations | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **3.60** | **3.20** | **4.37** | **4.13** | **3.86** | **3.83** |
| *2024 scores (CM)* | 3.96 | 3.34 | 4.47 | 4.21 | 3.91 | 3.98 |
| *2020 scores (CM)* | 2.80 | 3.23 | 4.63 | 3.95 | 3.75 | 3.67 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### SME Internationalisation

Given the relatively small size of most EaP countries' domestic markets, SMEs' success relies heavily on their ability to reach foreign markets. Unfortunately, obstacles including unequal access to information, financial constraints, and insufficient expertise can hinder SMEs' participation in international trade. This dimension assesses governments' support for SMEs with export-oriented endeavours.

Since the 2020 assessment, all EaP countries except for Armenia have improved their performance in this area. These efforts are reflected by the adoption of export promotion programmes, mainly facilitated by SME agencies, investment promotion agencies, and dedicated departments within Ministries of Economy. While currently there are no active export strategies in any of the EaP countries, most of them have adopted other relevant strategic policy documents. Common forms of support include the facilitation of trade missions, participation in trade fairs, and consultancy and advisory services. Moreover, all governments provide some form of financial support to exporting companies, although these measures differ in each country.

Overall, EaP governments need to establish more comprehensive monitoring and evaluation systems to enhance the effectiveness of export promotion programmes. Georgia is a leader in this regard, as it has a well-designed framework to monitor and evaluate the impacts of its services. Policy frameworks for SME integration into global value chains (GVCs) are in the early stages in most EaP countries. In Armenia, Moldova and Ukraine, although no systematic support is provided, proposals in this direction have been presented. In Azerbaijan, to support cluster development, eligible SMEs can apply to obtain substantial exemptions from different types of taxes for seven years. Again, Georgia at the forefront in this area, with established cluster policies and proactive assessments of changing GVCs.

The OECD Trade Facilitation Indicators indicate that the implementation of measures to facilitate EaP countries' business access to foreign markets has improved over time. However, while all EaP countries have enhanced their performance across the assessed areas, there are still performance gaps with OECD countries, specifically in areas related to documents, border agency co-operation, and procedures' automation.

All EaP countries have implemented a basic regulatory framework focused on policies to encourage e-commerce use by SMEs. However, alignment with EU frameworks could be improved, especially in regard to regulations on terms and conditions for accessing e-commerce platforms, on parcel delivery, and on consumer protection. Moreover, while all governments have designed measures to promote SMEs' use of e-commerce, the degree of their implementation varies. All countries, except Georgia, lack any form of a monitoring mechanism to assess the effectiveness of these measures.

Thus, moving forward, EaP countries should:

- Strengthen support for SME integration into GVCs by regularly assessing evolving GVCs, facilitating SME-MNC linkages, and incentivising foreign direct investment (FDI) to foster technology and financial transfers.

- Expand the regulatory framework by introducing provisions on consumer protection and regulations for paid advertisement in e-commerce.
- Automate and streamline trade-related procedures, including harmonising documents in line with international standards and improving internal and external border agency co-operation.
- Establish or enhance effective and transparent monitoring and evaluation mechanisms across all sub-dimensions to ensure continued efficiency and effectiveness.

### Table 2.10. Progress in the internationalisation dimension

| Internationalisation | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **2.91** | **3.25** | **4.52** | **3.45** | **3.77** | **3.58** |
| *2024 scores (CM)* | 2.82 | 3.33 | 4.66 | 3.70 | 3.60 | 3.62 |
| *2020 scores (CM)* | 2.98 | 3.20 | 3.76 | 2.87 | 2.75 | 3.11 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## *Pillar E: Innovation and Business Support*

SMEs often fall behind larger companies in terms of productivity, with relatively more pronounced gaps in the manufacturing sector. At the firm level, drivers of productivity performance relate to managerial and workforce skills and the adoption rate of innovations. SMEs can struggle in this regard, considering that they often face difficulties in obtaining information, offering training to their employees, accessing advanced consulting services and introducing new technologies. Innovation is also at the heart of the transition to a cleaner global environment, as improved processes and new technologies can make manufacturing more sustainable, reduce pollution and increase resource efficiency. Pillar E assesses policies promoting productivity, innovation and green practices in SMEs.

### Business development services

Business development services (BDS) cater to various topics, including information provision, training, consultancies and mentoring. They enhance competitiveness, efficiency and profitability by allowing entrepreneurs to start and operate businesses and by helping SMEs enter and explore new markets. However, these services need to adapt to evolving market conditions, technological advancements, and digitalisation trends. This dimension evaluates government initiatives designed to ensure that SMEs can access quality BDS and to address related market failures, with a sub-dimension focused on digital transformation support for SMEs.

The assessment for the BDS dimension results in a score of 3.57. On a comparable basis with the previous SBA assessment, this reflects an overall positive trend to enhance SME development services across the EaP region. Apart from Armenia, all countries bolstered their SME support agencies and expanded their services. Smaller countries, such as Moldova and Georgia, tend to manage support programmes directly through their SME agencies, whereas larger ones like Ukraine are opting for a more decentralised model leveraging external actors in the ecosystem for business support. The trend of countries strengthening SME support agencies is evident except in Armenia, where the government's overall capacity to assist SMEs has been reduced. Performance concerning the increasing role of private BDS providers has improved slightly across the EaP region, with Azerbaijan and Moldova demonstrating significant developments. Governments employ different strategies to engage private BDS providers, including outsourcing the provision of certain services to selected expert advisors (as in the case of Azerbaijan) or co-financing specialised consultancy costs (e.g. Georgia and Moldova). The EBRD's "Advice for Small Business" programme co-finances SME advisory projects and empowers local consultants through

training. According to the EBRD's data, most participating SMEs in EaP countries saw significant gains, including job creation and higher turnover rates.

Finally, regarding digital transformation, training in digital skills is the most common form of support provided by national SME agencies, although tailored analyses by specialised consultants of SMEs' digital needs are still missing. Some countries have started introducing full-fledged programmes for SME digitalisation (e.g. Moldova and Georgia), and potential partnerships with non-governmental actors should be explored to further SME digitalisation.

As EaP countries update their policy approaches to design and implement BDS for SMEs, the following recommendations could be taken into consideration:

- Include dedicated measures to deliver BDS for SMEs in governments' strategic documents.
- Ensure the sustainability of regional offices of SME agencies through strong quality-control mechanisms and cost/benefit analysis.
- Embed single information portals with information on all actors in the BDS ecosystem on SME agencies' websites, including donor-led initiatives and private quality-assured consultants.
- Develop a more market-based provision of BDS to SMEs by outsourcing support services to private BDS providers and increasing the offer of co-financing mechanisms to SMEs.
- Develop dedicated support programmes for SME digitalisation, including elements to enhance digital skills, company-specific digitalisation roadmaps, and financial tools to facilitate technology adoption.
- Improve the evaluation of business support programmes to assess the impact of BDS on various measures of SME performance.
- Monitor SME digitalisation by expanding the collection of statistical indicators on the adoption of digital technologies in the business sector.

### Table 2.11. Progress in the business development services dimension

| Business development services | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **3.06** | **3.33** | **4.22** | **3.69** | **3.57** | **3.57** |
| *2024 scores (CM)* | 3.27 | 3.81 | 4.35 | 4.01 | 3.27 | 3.74 |
| *2020 scores (CM)* | 4.10 | 3.12 | 4.30 | 3.70 | 2.80 | 3.61 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### Innovation policy

Although SMEs are crucial actors for generating and spreading innovations, their size may limit their capacity for sustained innovation. This dimension evaluates EaP governments' efforts to encourage SME innovation.

EaP countries show a slight improvement in this dimension compared to the previous assessment, achieving an average score of 3.09. The focus has shifted towards diversified financial support for innovative SMEs, notably in Ukraine. However, overarching policy frameworks for innovation, especially those tailored for SMEs, remain underdeveloped. While Moldova and Ukraine have dedicated national strategies, most countries incorporate innovation elements in broader documents. This deficiency is compensated by efforts to boost innovation in other ways, as observed in Armenia and Georgia's socio-economic strategies. Despite positive institutional shifts towards supporting business innovation, there is

large variation in the effectiveness of innovation agencies, with a notable scarcity of SME-specific initiatives and impact evaluations. Regarding institutional support, the expansion of in-kind services is apparent, often favouring the digital and IT sectors. Incubators and accelerators are widely present across the region, driven by both public and private entities. Science-industry linkages and technology transfer have gained some traction, as exemplified by Georgia and Ukraine, but their potential remains overall underutilised across the region. Government financial support for innovative SMEs has improved, mainly due to advancements in Armenia and Ukraine. However, the focus remains skewed towards the IT sector and start-ups. Grants are the primary direct financial support mechanism, varying in objectives and risk-sharing features. Despite EU funding programs being available, their engagement, particularly by SMEs, remains limited, and indirect financial incentives are scarce.

While renewing their policies to build a more innovative SME sector, EaP countries should focus on the following reform priorities:

- Highlight the role of SME innovation in strategic documents.
- Strengthen co-ordination and implementation capacity by identifying bodies tasked with supporting SME innovation and building staff capacity for dedicated programmes.
- Build the skills of agencies tasked with technology transfer and intensify co-operation between academia and the private sector to foster science-business linkages.
- Extend support beyond start-ups to mature SMEs and consider services to support technology absorption in more mature SMEs.
- Ensure that a matching component is required when awarding grants/soft loans, to share risks with beneficiaries of financial instruments for innovation.
- Introduce more flexible and market-based indirect financial incentives for innovation that are less prone to distortions and broaden the set of potential beneficiaries of support programmes.
- Strengthen the capacity of national statistical offices to collect information about SME innovation performance.

### Table 2.12. Progress in the innovation policy dimension

| Innovation | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **3.00** | **2.85** | **3.44** | **3.11** | **3.03** | **3.09** |
| *2024 scores (CM)* | 2.39 | 2.22 | 2.73 | 2.59 | 2.42 | 2.47 |
| *2020 scores (CM)* | 2.48 | 2.25 | 2.38 | 2.41 | 2.01 | 2.31 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### Green economy

Facilitating green SME practices can not only help in this regard, but can also boost competitiveness by reducing costs, enhancing market access and promoting technology adoption. This dimension evaluates government backing for greener SME practices using regulatory, financial and informational tools.

EaP countries have seen a slight increase in this dimension, achieving an average score of 2.81, with more pronounced improvements since the previous SBA assessment when comparing scores computed with comparable methodologies. However, environmental policies in most EaP countries policies rarely consider the specific needs of SMEs and financial incentives for green practices are not widespread. Moldova stands out as the leading performer in this dimension, due to its SME-focused environmental policies and its dedicated financial support programmes for greening SMEs. While all EaP countries acknowledge the importance of green initiatives for SMEs, concrete provisions in high-level planning

documents are limited. Moldova, Georgia, and to a lesser extent, Armenia, have provisions for SMEs in their strategic policies. Other countries lack specific targets, potentially overlooking SME-specific barriers to improved environmental performance. Implementation-wise, SME agencies rarely promote green initiatives. Moldova is an exception, with its local SME agency (ODA) playing a prominent role in promoting greening practices directly to entrepreneurs. Financial support for SME greening is often reliant on donor funding. Progress has been observed across all EaP countries regarding the availability of tools and instruments supporting SMEs in adopting green practices. Environmental regulations are evolving, such as Armenia's risk-based environmental impact assessments. Moldova employs deterrents like tax measures and environmental pollution charges. While environmental management systems are being promoted, there is only limited financial support for SMEs (except in Moldova). Green public procurement exists, but its impact on SMEs is uncertain.

To advance their policy frameworks for supporting greener SMEs, EaP governments could consider the following reform priorities:

- Adapting national green economy policies and targets to SMEs.
- Enhancing institutional capacity to provide guidance and support to SMEs – which, in turn, will raise awareness and assist SMEs in their transition toward environmentally friendly practices.
- Emphasising the business case for improving environmental performance. Government agencies could leverage a diversity of intermediaries to enhance outreach to SMEs.
- Facilitating partnerships and best-practice sharing among businesses to support SME greening activities.
- Creating a demand for greener products, services, and production processes, ensuring that public procurement policies adopt green/sustainable assessment criteria in their tenders.
- Increasing the availability of financing instruments for investing in greener equipment and processes.
- Improving the statistical production of environmental indicators to strengthen tools to evaluate the impact of SME greening policies, certification and support programmes on actual SME environmental performance.

### Table 2.13. Progress in the green economy dimension

| Green economy | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| 2024 scores | **2.51** | **2.54** | **3.08** | **3.38** | **2.56** | **2.81** |
| *2024 scores (CM)* | 2.80 | 2.52 | 3.27 | 3.74 | 2.61 | 2.99 |
| *2020 scores (CM)* | 2.43 | 2.15 | 2.74 | 3.16 | 2.49 | 2.59 |

Note: CM stands for Comparable Methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *Key findings for each country*

**Armenia,** despite challenges, experienced remarkable economic growth. In 2022, the country's GDP surged by 12.6%, primarily fuelled by investment, domestic consumption and the tertiary sector. The large influx of businesses and individuals from Russia contributed substantially to the economic growth. Exports of goods grew by 75% in 2022, driven by shifts in regional supply chains. The importance of industry and agriculture in Armenia's economy has been steadily decreasing, while the ICT sector has recently been expanding, including because of an influx of skilled labour from Russia. As of 2021, SMEs accounted for nearly 99.9% of all businesses in the economy, with micro-enterprises making up 94.7% (Armstat, 2022[4]).

In 2021, SMEs contributed 69.6% to overall business employment and generated up to 63% of the value added in the business sector.

### Table 2.14. Overview of Armenia's key reforms since 2020 and recommendations

| Key reforms | Key recommendations |
|---|---|
| Adopted an SME Development Strategy for 2020-2024 and a National Digitalisation Strategy for 2021-2025<br>Provided training from 2021-2022 for teachers in general education on technology and entrepreneurship<br>Launched an Economic Modernisation Program for interest rate subsidies on loans and leases to purchase modern (new) equipment<br>Improved services on standardisation, metrology and conformity assessment<br>Made the use of e-procurement mandatory<br>Introduced a pilot project to collect data on SME adoption of digital technologies and created a programme to help start-ups | Ensure and monitor implementation of the National Digitalisation Strategy<br>Improve tax compliance, accelerate regulatory reforms and enhance RIA application<br>Streamline bankruptcy procedures, introduce out-of-court debt restructuring options, and promote a second chance policy<br>Collect data on SME skills and women's entrepreneurship, and improve co-ordination among support providers<br>Encourage bank lending to SMEs by streamlining enforcement processes and enhancing their efficiency<br>Identify a co-ordinating agency for SME services, focus on policy coherence, and consolidate innovation support<br>Develop a comprehensive strategy to promote green practices among SMEs |

**Azerbaijan**, a major hydrocarbon exporter, saw its GDP grow by 4.7% in 2022, benefiting from rising oil and gas prices driven by Russia's invasion of Ukraine. This bolstered the country's post-COVID-19 recovery, despite inflation reaching nearly 14% in 2022. The mining and quarrying sector continues to dominate, with the extraction of crude petroleum and natural gas accounting for 45% of value added in 2022, while agriculture employed over a third of the workforce but contributed only 4.8% of value added in 2022. The economic potential of SMEs remains largely untapped: in 2021, they generated 16.4% of value added and accounted for 41.8% of total employment (SSCRA, 2022[5]). Azerbaijan has the potential to harness digital transformation to diversify its economy.

### Table 2.15. Overview of Azerbaijan's key reforms since 2020 and recommendations

| Key reforms | Key recommendations |
|---|---|
| Included SME measures in the Socio-economic Development Strategy 2022-2026 and amended the Insolvency Law<br>Established women resource centres in regions<br>Developed a framework to collect and analyse data on SME skills and a network of operators to step up training provisions<br>Implemented Basel III principles<br>Established an online sales platform to support SME exports<br>Outreach and financial support to SMEs ensured through KOBIA's network of sub-structures | Ensure that the upcoming NDS adopts a comprehensive approach for digital transformation in non-IT sectors<br>Complement the National Socio-economic Development Strategy with a comprehensive SME strategy<br>Incorporate entrepreneurship as a key competence across education levels<br>Improve the legal framework for secure transactions and promote non-bank financing options for SMEs<br>Introduce financial support mechanisms to support exporting SMEs and provide trade insurance services<br>Improve monitoring practices by assessing the impact of selected support programmes on beneficiaries' performance |

**Georgia**'s economy remained resilient despite short-term disruptions caused by Russia's invasion of Ukraine. The country's GDP grew by 10.1% in 2022, supported by an influx of skilled migrant workers, business relocations from Russia, and increased transportation flows. Inflation, which had been high since 2021, decreased to 0.6% in June 2023 due to effective policy measures. Georgia's foreign trade turnover increased by 33.4% in 2022, with a focus on exports like copper ores, cars and wine. The ICT sector contributed 4.7% to GDP and grew by 49.9% in 2022. In 2021, small businesses represented 98.2% of the business population, whereas medium-sized enterprises accounted for 1.5%. Although SMEs' employment levels are still lower than pre-pandemic levels, they represent 61.8% of the business sector workforce. SMEs' value added has increased over 2015-2021, but their share of total business sector value added has remained between 53% and 61% over that period, falling to 53% in 2021.

### Table 2.16. Overview of Georgia's key reforms since 2020 and recommendations

| Key reforms | Key recommendations |
|---|---|
| Adopted an SME Development Strategy for 2021-2025, with new priorities for women's entrepreneurship and the green economy<br>Created a Skills Agency, notably launching teacher networks to stimulate VET partnerships<br>Expanded the national credit guarantee scheme following the pandemic<br>Export assistance programme and growth hubs launched by Enterprise Georgia to support SMEs with training, services and financing, along with significant improvements in monitoring and evaluation<br>Established an independent Market Surveillance Agency | Adopt a National Digital Strategy<br>Explore initiatives to promote a second chance for bankrupt entrepreneurs, including incentives and dedicated programmes<br>Integrate entrepreneurship into education at all education levels, enhance teacher training, and improve monitoring and evaluation.<br>Implement collateral/factoring reforms and larger-scale start-up funding<br>Revise the e-procurement system to align with EU directives and improve data quality<br>Consider indirect financial incentives for innovation and research and development (R&D)<br>Develop reporting requirements on firm size within ESG reporting frameworks to monitor impact of green finance policies on SMEs |

**Moldova** has faced several crises in recent years, including the COVID-19 pandemic and severe droughts in 2020, which resulted in recession. Although the country rebounded with 13.9% growth in 2021, Russia's war of aggression against Ukraine in 2022 brought new challenges – including trade disruptions, a significant influx of refugees, and high inflation – which resulted in a contraction of the economy of 5.6%. Moldova, seeking to reduce its dependence on Russian gas, witnessed soaring energy prices, contributing to inflation levels of up to 34% in 2022. SMEs accounted for 59% of business sector employment and 38% of turnover in 2021. Their share in low-value-added sectors, albeit predominant, has been decreasing, while the country has the second-highest share of SMEs in the ICT sector among EaP countries (5% of total SMEs in 2021). Fostering SME growth and promoting a competitive market will help address the challenges posed by rising costs and labour shortages.

### Table 2.17. Overview of Moldova's key reforms since 2020 and recommendations

| Key reforms | Key recommendations |
|---|---|
| Developed the National Programme for Promoting Entrepreneurship and Increasing Competitiveness 2022-26 (PACC)<br>Efforts to align Education Code with European key competences and progress in non-formal learning<br>Launch of the Investment incentive programme "373"<br>Adopted a State Programme for SME growth and internationalisation<br>Successful launch and implementation of new comprehensive programmes to support the digital transformation of SMEs as well as digital Innovations and technological start-ups | Ensure implementation and effective monitoring and evaluation (M&E) of the new National Digital Strategy<br>Introduce SME-focused RIA test<br>Enhance skills assessment and anticipation by collecting data on SME skills, needs, and in-house training, sharing results on an online database<br>Promote alternative financing, explore VC sector options, and improve financial literacy of entrepreneurs<br>Update MTender and raise user skills to better align with regulatory requirements and options<br>Enhance SME access to external advisors, introduce incentives for R&D and innovation investment, encourage green practices among SMEs and enhance data collection on their environmental and greening performance |

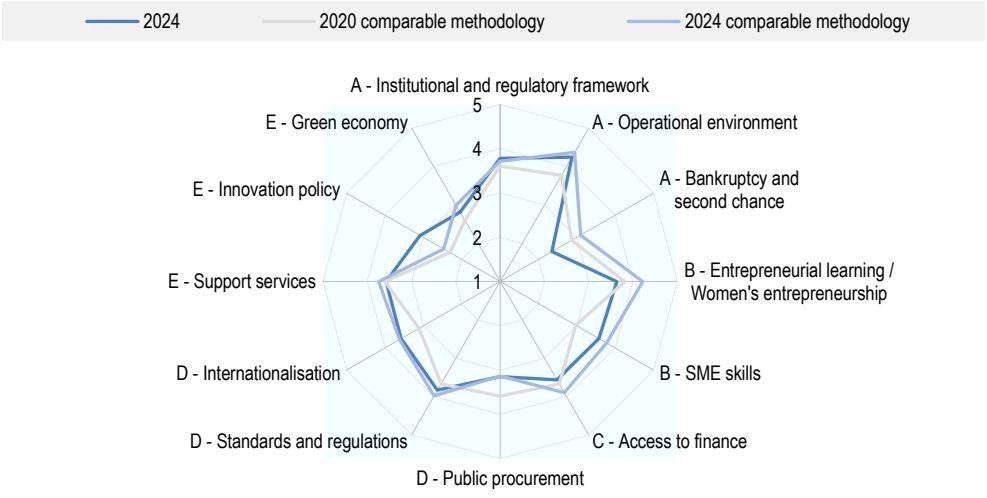
**Ukraine** has faced severe challenges in recent years, including a 3.8% GDP decline in 2020 due to COVID-19 and a 29.1% GDP contraction caused by Russia's war of aggression in 2022. Despite this, the country's economy has shown resilience, with 2023 growth estimated at 2-3% in mid-2023. Exports have dropped by around 43%, with transport issues posing major challenges to businesses. While Ukraine's banking system has remained resilient, non-performing loans have grown to 38%. International aid has played a crucial role, with financial assistance needs estimated at USD 36-48 billion in 2023. SMEs, which constituted 99.98% of all enterprises in the business sector in 2021, accounted for 81.6% of the total business employment in Ukraine and generated 70.2% of value added at factor cost in the business sector that year (State Statistics Service of Ukraine, 2023[6]). The digitalisation process, already a policy priority before the war, has advanced, and the IT sector has been showing impressive resilience in wartime.

## Table 2.18. Overview of Ukraine's key reforms since 2020 and recommendations

| Key reforms | Key recommendations |
|---|---|
| Launched the Diia.Business web-portal, thereby helping SMEs and entrepreneurs<br>Public and private training opportunities for SMEs enhanced, including for women entrepreneurs<br>SMEs' access to finance enhanced through the government's "5-7-9%" loans programme<br>Order No. 285 of Ukraine's National Standardization Body "On the package adoption of the CEN-CENELEC European regulatory documents by Ukraine" to adopt 20,268 European CEN/CENELEC normative documents as national normative documents by December 31, 2023<br>Established a Ukrainian Startup Fund and developed a network of Diia.Business support centres | Align the post-war SME strategy with reconstruction plans, streamline regulations, and prioritise deregulation<br>Establish a systematic approach to skills assessment and anticipation, improving data collection and labour market analyses<br>Strengthen non-bank financing by updating the legal framework for factoring and encouraging VC<br>Enhance public procurement for SMEs<br>Introduce grants for facilitating access to private BDS providers and refine evaluation of support schemes<br>Implement measures to stimulate business innovation, adjusting existing incentives to the needs of SMEs<br>Develop a dedicated SME greening strategy and reinforce environmental policies for sustainable growth |

### *Overview of regional performance*

## Figure 2.2. Progress towards SME supportive policies in EaP countries, 2020 and 2024




Note: Overall dimension scores are calculated based on five levels of policy reform, with 1 being the weakest and 5 being the strongest. Methodological changes have been introduced to the 2024 assessment based on lessons learnt from previous SBA assessments and to capture important changes and emerging trends in the business and policy environment. Only scores calculated according to a comparable methodology should be compared to identify trends over time. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Since the last SBA assessment in 2020, EaP countries' performance has improved across all dimensions (except public procurement), particularly with regard to the operational environment and to SME skills. These results show the governments' commitment to reducing the burden on businesses by providing efficient government services and reducing the cost of administrative procedures and regulatory requirements, as well as their efforts directed at addressing skills shortages and mismatches (Table 2.19) provides an overview of the region's progress for each SBA dimension since the assessment conducted in 2020.

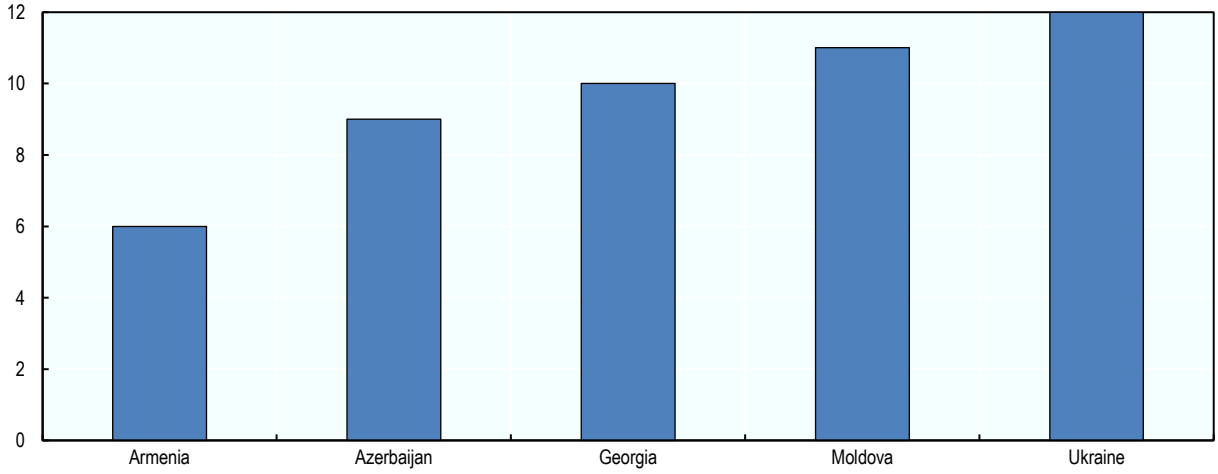
## Table 2.19. Summary of regional progress in SME policy development

| Pillar | Dimension | 2024 EaP Average | 2024 CM EaP Average | 2020 CM EaP Average | Change 2020-24 (CM) |
|---|---|---|---|---|---|
| A | Institutional and regulatory framework | 3.78 | 3.72 | 3.61 | +0.11 |
| | Operational environment | 4.24 | 4.37 | 3.77 | +0.60 |
| | Bankruptcy and second chance | 2.35 | 3.10 | 2.87 | +0.23 |
| B | Entrepreneurial learning / women's entrepreneurship | 3.64 | 4.22 | 3.81 | +0.41 |
| | SME skills | 3.57 | 3.78 | 2.97 | +0.79 |
| C | Access to finance | 3.56 | 3.90 | 3.67 | +0.23 |
| D | Public procurement | 3.15 | 3.13 | 3.59 | -0.46 |
| | Standards and regulations | 3.83 | 3.98 | 3.67 | +0.31 |
| | Internationalisation | 3.58 | 3.62 | 3.11 | +0.51 |
| E | Business development services | 3.57 | 3.74 | 3.61 | +0.13 |
| | Innovation policy | 3.09 | 2.47 | 2.31 | +0.16 |
| | Green economy | 2.81 | 2.99 | 2.59 | +0.40 |

Note: CM = Comparable methodology. Darker blue colouring denotes a higher rate of change during 2020-24. Methodological changes have been introduced to the 2024 assessment based on lessons learnt from previous SBA assessments and to capture important changes and emerging trends in the business and policy environment. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Developments in the EaP region's SME environment have been diverse. Overall, progress in Pillar B, *Entrepreneurial human capital*, is the highest on average, reflecting EaP countries' efforts to help citizens acquire and develop entrepreneurial skills and competences. Significant improvements have also been achieved in Pillar A, *Responsive government*, where, as mentioned above, the increase in average scores has been driven mostly by improvements in the *operational environment* for SME. On the other hand, the weakest advancements can be observed in Pillar D, *Access to markets*, where the major improvements in support to SME *internationalisation* are counterbalanced by significant setbacks in *public procurement*. In fact, while all EaP countries recognise the importance of SME internationalisation and have adopted a strategic approach to export promotion and the use of e-commerce, the results of the assessment show a deterioration in the regulatory framework for public procurement. Figure 2.3 shows, for each country, the number of dimensions where the scores have improved since the 2020 assessment.

## Figure 2.3. Improvements by number of dimensions by EaP country




Note: To calculate the number of dimensions where the scores have improved since 2020, scores calculated using comparable methodology were considered. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Despite extremely difficult circumstances – due initially to the COVID-19 pandemic and then, more significantly, to Russia's full-scale invasion in February 2022 – Ukraine confirmed its top position as best reformer among EaP countries, having improved across all 12 dimensions of the assessment. Moldova followed suit, displaying improvements in 11 dimensions.

Table 2.20 indicates for each country the areas of best performance and the areas with the biggest margin for improvement.

### Table 2.20. Summary of each country's progress and main areas for improvement

| Country | Stronger performance | Score | Main areas for improvement | Score |
|---|---|---|---|---|
| Armenia | Pillar A - Operational environment | 3.99 | Pillar A - Bankruptcy and second chance | 1.97 |
| | Pillar D - Standards and regulations | 3.60 | Pillar B - SME skills | 2.37 |
| | Pillar C - Access to finance | 3.54 | Pillar E - Green economy | 2.51 |
| Azerbaijan | Pillar A - Operational environment | 4.25 | Pillar A - Bankruptcy and second chance | 1.91 |
| | Pillar A - Institutional framework | 3.69 | Pillar E - Green economy | 2.54 |
| | Pillar B - SME skills | 3.59 | Pillar D - Public procurement | 2.55 |
| Georgia | Pillar D - Internationalisation | 4.52 | Pillar E - Green economy | 3.08 |
| | Pillar A - Operational environment | 4.51 | Pillar A - Bankruptcy and second chance | 3.36 |
| | Pillar A - Institutional framework | 4.37 | Pillar E - Innovation policy | 3.44 |
| Moldova | Pillar A - Operational environment | 4.34 | Pillar A - Bankruptcy and second chance | 2.00 |
| | Pillar D - Standards and regulations | 4.13 | Pillar E - Innovation policy | 3.11 |
| | Pillar B - Entrepreneurial learning / women's entrepreneurship | 4.09 | Pillar D - Public procurement | 3.16 |
| Ukraine | Pillar A - Operational environment | 4.11 | Pillar A - Bankruptcy and second chance | 2.52 |
| | Pillar B - Entrepreneurial learning / women's entrepreneurship | 3.95 | Pillar E - Green economy | 2.56 |
| | Pillar B - SME skills | 3.91 | Pillar E - Innovation policy | 3.03 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## 2024 SME Policy Index scores for Eastern Partner countries

Table 2.22 shows the 2024 SME Policy Index scores for each EaP country, with Box 2.1 summarising the scoring methodology.

The SME Policy Index aims at providing governments with guidance on evaluating policies targeting SME development. The index identifies strengths and weaknesses in policy design, implementation, monitoring and evaluation; allows for comparison across countries; and measures convergence towards good SME policy practices promoted by the EU and the OECD. It assists governments in setting targets for SME policy development and strategic priorities to further improve their business environments. It also fosters governments' policy dialogue, including with the private sector, and facilitates peer exchanges across the region and with partner organisations.

### Box 2.1. Scoring SME policy development

The SME Policy Index is calculated considering both qualitative information and quantitative outcome-oriented indicators. The qualitative indicators assess the policy development path in a certain area, such as the establishment of a regulatory impact assessment or a credit guarantee scheme. The outcome-oriented indicators are collected to strengthen the link between policies and outcomes. The analysis was also enriched by evidence gathered through private sector focus groups organised in the framework of this fourth assessment round.

Scores between 1 and 5 are used to assess the level of policy reform for each sub-dimension and dimension, with 1 being the weakest level and 5 being the strongest. For qualitative indicators, the scores typically correspond to the levels of policy development shown in Table 2.21.

#### Table 2.21. Policy development scale

| Level 1 | Level 2 | Level 3 | Level 4 | Level 5 |
|---|---|---|---|---|
| There is no law, institution, tool or (information) service in place for the area concerned. | There is a draft law, institution, tool or (information) service and there are some signs of government activity to address the area concerned. | A solid legal and/or institutional framework is in place for this specific policy area, tool or (information) service. | Level 3 complemented by some concrete indications of effective policy implementation of the law, institution or tool. | Level 4 complemented by significant evidence of concrete and effective policy implementation of the law, institution, tool or service. This level comes closest to good practice identified for the OECD countries. |

A detailed description of the policy framework and process underpinning the assessment is provided in the chapter "Policy framework, structure of the report and assessment process". The scoring methodology is provided in Annex A.

#### Table 2.22. 2024 SME Policy Index scores in the EaP countries

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | Weight |
|---|---|---|---|---|---|---|---|
| **Digital economy for SMEs** | | | | | | | |
| **Composite score for SME digitalisation** | **3.44** | **3.14** | **3.96** | **3.40** | **3.77** | **3.54** | |
| *Selected framework conditions for the digital transformation* | *3.92* | *2.96* | *4.02* | *3.22* | *3.93* | *3.61* | |
| **Pillar A – Responsive government** | | | | | | | |
| **Institutional and regulatory framework** | **3.24** | **3.69** | **4.37** | **3.93** | **3.68** | **3.78** | |
| **Institutional setting** | **3.02** | **4.14** | **4.62** | **3.83** | **3.70** | **3.86** | **40%** |
| *Planning and design* | 3.47 | 4.07 | 4.73 | 4.00 | 4.05 | 4.06 | 35% |
| *Implementation* | 2.63 | 4.52 | 4.71 | 3.71 | 3.38 | 3.79 | 45% |
| *Monitoring and evaluation* | 3.13 | 3.40 | 4.20 | 3.80 | 3.80 | 3.67 | 20% |
| **Legislative simplification and RIA** | **3.03** | **2.90** | **3.50** | **3.35** | **3.27** | **3.21** | **25%** |
| *Planning and design* | 4.13 | 3.40 | 4.53 | 4.00 | 4.20 | 4.05 | 35% |
| *Implementation* | 2.13 | 2.22 | 2.15 | 2.24 | 2.14 | 2.18 | 45% |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | Weight |
|---|---|---|---|---|---|---|---|
| *Monitoring and evaluation* | 3.13 | 3.53 | 4.73 | 4.73 | 4.20 | 4.07 | 20% |
| **Public-private consultations** | **4.16** | **3.40** | **4.65** | **4.27** | **4.26** | **4.15** | **15%** |
| *Frequency and transparency of PPCs* | 4.33 | 3.11 | 4.67 | 4.50 | 4.42 | 4.20 | 40% |
| *Private sector involvement in PPCs* | 4.07 | 3.40 | 4.96 | 3.67 | 4.73 | 4.16 | 40% |
| *Monitoring and evaluation* | 4.00 | 4.00 | 4.00 | 5.00 | 3.00 | 4.00 | 20% |
| **Institutional framework for SME digitalisation** | **3.50** | **4.05** | **4.54** | **4.20** | **4.40** | **4.14** | **10%** |
| **Outcome-oriented indicators** | **3.00** | **4.00** | **5.00** | **5.00** | **3.00** | **4.00** | **10%** |
| **Operational environment** | **3.99** | **4.25** | **4.51** | **4.34** | **4.11** | **4.24** | |
| **E-government services** | **4.00** | **4.25** | **4.29** | **4.34** | **4.66** | **4.31** | **35%** |
| *Strategy, planning and design* | 3.93 | 4.30 | 4.92 | 4.82 | 4.56 | 4.51 | 35% |
| *Implementation* | 4.21 | 4.33 | 4.36 | 4.42 | 4.88 | 4.44 | 45% |
| *Monitoring and evaluation* | 3.67 | 4.00 | 3.00 | 3.33 | 4.33 | 3.67 | 20% |
| **Business licenses** | **3.66** | **3.96** | **5.00** | **4.69** | **4.40** | **4.34** | **10%** |
| *Licence procedures* | 4.14 | 4.43 | 5.00 | 4.43 | 4.83 | 4.57 | 40% |
| *Monitoring and streamlining of licence systems* | 3.33 | 3.64 | 5.00 | 4.87 | 4.11 | 4.19 | 60% |
| **Company registration** | **4.88** | **4.52** | **5.00** | **4.74** | **4.52** | **4.73** | **25%** |
| *Design and implementation* | 4.80 | 4.20 | 5.00 | 4.90 | 4.20 | 4.62 | 60% |
| *Monitoring and evaluation* | 5.00 | 5.00 | 5.00 | 4.50 | 5.00 | 4.90 | 40% |
| **Tax compliance procedures** | **2.73** | **3.70** | **4.26** | **3.78** | **2.73** | **3.44** | **20%** |
| *Tax compliance and simplification procedures* | 3.12 | 3.59 | 4.53 | 3.35 | 3.12 | 3.54 | 60% |
| *Monitoring and evaluation of SME-specific tax measures* | 2.14 | 3.86 | 3.86 | 4.43 | 2.14 | 3.29 | 40% |
| **Outcome-oriented indicators** | **4.56** | **5.00** | **4.11** | **4.11** | **3.67** | **4.29** | **10%** |
| **Bankruptcy and second chance** | **1.97** | **1.91** | **3.36** | **2.00** | **2.52** | **2.35** | |
| **Preventive measures** | **1.34** | **1.69** | **3.24** | **1.46** | **1.75** | **1.90** | **30%** |
| *Design and implementation* | 1.86 | 2.71 | 3.60 | 2.14 | 2.89 | 2.64 | 40% |
| *Performance, monitoring and evaluation* | 1.00 | 1.00 | 3.00 | 1.00 | 1.00 | 1.40 | 60% |
| **Survival and bankruptcy procedures** | **2.74** | **2.15** | **4.13** | **2.72** | **3.39** | **3.03** | **40%** |
| *Design and implementation* | 3.35 | 3.88 | 4.33 | 3.80 | 3.96 | 3.87 | 40% |
| *Performance, monitoring and evaluation* | 2.33 | 1.00 | 4.00 | 2.00 | 3.00 | 2.47 | 60% |
| **Promoting second chance** | **1.00** | **1.33** | **2.33** | **1.00** | **1.83** | **1.50** | **20%** |
| **Outcome-oriented indicators** | **2.71** | **2.71** | **2.71** | **2.71** | **2.71** | **2.71** | **10%** |
| **Pillar B – Entrepreneurial human capital** | | | | | | | |
| **Entrepreneurial learning/women's entrepreneurship** | **2.91** | **3.07** | **4.17** | **4.09** | **3.95** | **3.64** | |
| **Entrepreneurial learning** | **3.10** | **2.88** | **3.87** | **4.14** | **4.01** | **3.60** | **55%** |
| *Planning and design* | 3.87 | 3.53 | 4.33 | 5.00 | 4.53 | 4.25 | 30% |
| *Implementation* | 2.90 | 2.73 | 3.64 | 3.91 | 4.05 | 3.45 | 50% |
| *Monitoring and evaluation* | 2.47 | 2.26 | 3.76 | 3.40 | 3.10 | 3.00 | 20% |
| **Women's entrepreneurship** | **2.50** | **3.71** | **4.90** | **4.40** | **4.21** | **3.94** | **35%** |
| *Planning and design* | 4.43 | 3.57 | 5.00 | 5.00 | 4.14 | 4.43 | 30% |
| *Implementation* | 1.53 | 3.80 | 5.00 | 4.20 | 4.33 | 3.77 | 50% |
| *Monitoring and evaluation* | 2.00 | 3.70 | 4.50 | 4.00 | 4.00 | 3.64 | 20% |
| **Outcome-oriented indicators** | **3.29** | **1.86** | **3.29** | **2.71** | **2.71** | **2.77** | **10%** |
| **SME skills** | **2.37** | **3.59** | **4.12** | **3.89** | **3.91** | **3.57** | |
| **SME skills** | **2.41** | **3.76** | **4.25** | **4.10** | **4.01** | **3.71** | **90%** |
| *Planning and design* | 1.67 | 3.13 | 4.49 | 4.69 | 3.39 | 3.47 | 30% |
| *Implementation* | 2.75 | 4.00 | 3.80 | 4.00 | 4.75 | 3.86 | 50% |
| *Monitoring and evaluation* | 2.67 | 4.11 | 5.00 | 3.44 | 3.11 | 3.67 | 20% |
| **Outcome-oriented indicators** | **2.00** | **2.00** | **3.00** | **2.00** | **3.00** | **2.40** | **10%** |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | Weight |
|---|---|---|---|---|---|---|---|
| **Pillar C – Access to finance** | | | | | | | |
| **Access to finance** | **3.54** | **3.31** | **4.07** | **3.48** | **3.40** | **3.56** | |
| **Legal and regulatory framework** | **4.03** | **4.13** | **4.31** | **4.33** | **3.70** | **4.10** | **35%** |
| *Creditor rights* | 3.20 | 4.10 | 4.10 | 5.00 | 3.20 | 3.92 | 24% |
| *Register* | 4.86 | 4.91 | 5.00 | 4.81 | 4.90 | 4.90 | 24% |
| *Credit information bureau* | 4.32 | 4.32 | 4.32 | 4.32 | 4.32 | 4.32 | 24% |
| *Banking regulations* | 3.40 | 2.90 | 4.09 | 3.00 | 1.26 | 2.93 | 14% |
| *Capital market* | 4.16 | 3.71 | 3.71 | 3.71 | 3.89 | 3.84 | 14% |
| **Sources of external finance - bank financing** | **2.30** | **2.34** | **3.74** | **2.67** | **2.54** | **2.72** | **25%** |
| *Banking lending practices and conditions* | 2.66 | 2.32 | 3.31 | 2.66 | 2.50 | 2.69 | 60% |
| *Credit guarantee schemes* | 1.78 | 2.38 | 4.38 | 2.70 | 2.61 | 2.77 | 40% |
| **Sources of external finance – non-bank financing** | **4.56** | **3.61** | **3.71** | **4.04** | **4.22** | **4.03** | **15%** |
| *Microfinance institutions* | 4.40 | 4.08 | 5.00 | 4.64 | 4.60 | 4.54 | 33% |
| *Leasing* | 4.71 | 3.51 | 5.00 | 4.71 | 5.00 | 4.59 | 33% |
| *Factoring* | 4.70 | 3.35 | 1.25 | 2.90 | 3.20 | 3.08 | 33% |
| **Venture capital ecosystem** | **3.34** | **2.04** | **3.56** | **2.32** | **2.52** | **2.75** | **5%** |
| *Legal framework* | 3.78 | 3.44 | 4.11 | 3.44 | 3.44 | 3.64 | 35% |
| *Design and implementation of government activities* | 3.75 | 1.40 | 3.67 | 2.04 | 2.47 | 2.66 | 45% |
| *Monitoring and evaluation* | 1.67 | 1.00 | 2.33 | 1.00 | 1.00 | 1.40 | 20% |
| **Financial literacy** | **4.53** | **3.27** | **4.80** | **2.94** | **3.94** | **3.90** | **5%** |
| *Planning, design and implementation* | 4.75 | 3.50 | 4.75 | 3.10 | 3.94 | 4.01 | 80% |
| *Monitoring and evaluation* | 3.67 | 2.33 | 5.00 | 2.33 | 3.93 | 3.45 | 20% |
| **Digital financial services** | **3.52** | **3.05** | **3.94** | **3.02** | **3.81** | **3.47** | **5%** |
| *Regulatory frameworks for digital financial services* | 3.74 | 3.60 | 4.37 | 3.55 | 4.11 | 3.87 | 50% |
| *Supervisory framework for digital financial services* | 3.30 | 2.50 | 3.50 | 2.50 | 3.50 | 3.06 | 50% |
| **Pillar D – Access to markets** | | | | | | | |
| **Public procurement** | **2.80** | **2.55** | **3.61** | **3.16** | **3.61** | **3.15** | |
| **Public procurement** | **3.00** | **2.72** | **3.68** | **3.40** | **3.58** | **3.28** | **90%** |
| *Policy and regulatory framework* | 2.75 | 2.43 | 3.09 | 3.75 | 3.42 | 3.09 | 35% |
| *Implementation* | 4.09 | 2.83 | 4.43 | 4.20 | 3.51 | 3.81 | 45% |
| *Monitoring and evaluation* | 1.00 | 3.00 | 3.00 | 1.00 | 4.00 | 2.40 | 20% |
| **Outcome-oriented indicators** | **1.00** | **1.00** | **3.00** | **1.00** | **3.86** | **1.97** | **10%** |
| **Standards and regulations** | **3.60** | **3.20** | **4.37** | **4.13** | **3.86** | **3.83** | |
| **Overall co-ordination and general measures** | **5.00** | **3.23** | **5.00** | **4.33** | **5.00** | **4.51** | **10%** |
| **Harmonisation with EU acquis** | **3.58** | **3.30** | **4.42** | **3.94** | **4.40** | **3.93** | **40%** |
| *Technical regulations* | 4.10 | 3.14 | 4.36 | 4.10 | 4.42 | 4.02 | 16.7% |
| *Standardisation* | 4.25 | 3.30 | 4.49 | 4.05 | 3.67 | 3.95 | 16.7% |
| *Accreditation* | 3.61 | 3.84 | 4.36 | 4.36 | 4.80 | 4.19 | 16.7% |
| *Conformity assessment* | 2.76 | 3.40 | 4.19 | 4.29 | 4.68 | 3.87 | 16.7% |
| *Metrology* | 4.78 | 3.35 | 4.47 | 3.80 | 4.73 | 4.23 | 16.7% |
| *Market surveillance* | 1.94 | 2.76 | 4.60 | 3.00 | 4.04 | 3.27 | 16.7% |
| **SME access to standardisation** | **3.85** | **3.25** | **4.13** | **4.55** | **2.83** | **3.72** | **30%** |
| *Awareness raising and information* | 4.33 | 4.17 | 4.25 | 4.83 | 3.92 | 4.30 | 30% |
| *SMEs' participation in developing standards* | 4.50 | 4.00 | 4.50 | 5.00 | 3.50 | 4.30 | 30% |
| *Financial support to SMEs* | 3.00 | 2.00 | 3.75 | 4.00 | 1.50 | 2.85 | 40% |
| **Digitalisation of standards and regulations** | **1.50** | **2.13** | **3.63** | **2.50** | **2.50** | **2.45** | **10%** |
| **Outcome-oriented indicators** | **3.67** | **3.67** | **5.00** | **5.00** | **5.00** | **4.47** | **10%** |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | Weight |
|---|---|---|---|---|---|---|---|
| **SME internationalisation** | **2.91** | **3.25** | **4.52** | **3.45** | **3.77** | **3.58** | |
| **Export promotion** | **3.57** | **3.67** | **4.84** | **4.28** | **4.30** | **4.13** | **40%** |
| *Planning and design* | 3.90 | 4.50 | 4.75 | 4.75 | 4.80 | 4.54 | 35% |
| *Implementation* | 3.62 | 3.92 | 4.85 | 3.92 | 3.77 | 4.02 | 45% |
| *Monitoring and evaluation* | 2.89 | 1.64 | 5.00 | 4.27 | 4.64 | 3.69 | 20% |
| **Integration into global value chains** | **1.23** | **2.16** | **4.80** | **2.77** | **3.76** | **2.94** | **20%** |
| *Planning and design* | 1.65 | 2.22 | 4.63 | 2.19 | 4.69 | 3.08 | 35% |
| *Implementation* | 1.00 | 2.33 | 4.83 | 2.83 | 3.67 | 2.93 | 45% |
| *Monitoring and evaluation* | 1.00 | 1.67 | 5.00 | 3.67 | 2.33 | 2.73 | 20% |
| **OECD Trade Facilitation Indicators** | **3.88** | **3.60** | **4.22** | **3.22** | **3.15** | **3.62** | **10%** |
| **Use of e-commerce** | **2.25** | **3.44** | **4.00** | **3.31** | **2.89** | **3.18** | **20%** |
| *Planning and design* | 3.70 | 3.83 | 4.00 | 4.43 | 4.10 | 4.01 | 35% |
| *Implementation* | 1.67 | 4.00 | 4.00 | 3.47 | 2.33 | 3.09 | 45% |
| *Monitoring and evaluation* | 1.00 | 1.50 | 4.00 | 1.00 | 2.00 | 1.90 | 20% |
| **Outcome-oriented indicators** | **4.00** | **3.00** | **4.00** | **2.00** | **4.00** | **3.40** | **10%** |
| **Pillar E – Innovation and business support** | | | | | | | |
| **Business development services** | **3.06** | **3.33** | **4.22** | **3.69** | **3.57** | **3.57** | |
| **Services provided by government** | **3.38** | **3.96** | **4.51** | **4.17** | **4.08** | **4.02** | **40%** |
| *Planning and design* | 3.55 | 3.55 | 5.00 | 4.27 | 4.27 | 4.13 | 35% |
| *Implementation* | 3.33 | 4.39 | 4.39 | 4.28 | 4.50 | 4.18 | 45% |
| *Monitoring and evaluation* | 3.18 | 3.73 | 3.91 | 3.73 | 2.82 | 3.47 | 20% |
| **Initiatives to stimulate private BDS** | **3.14** | **3.19** | **4.10** | **3.72** | **3.20** | **3.47** | **40%** |
| *Planning and design* | 3.00 | 2.60 | 3.93 | 4.20 | 3.33 | *3.41* | 35% |
| *Implementation* | 3.31 | 3.44 | 4.33 | 3.67 | 3.49 | *3.65* | 45% |
| *Monitoring and evaluation* | 3.00 | 3.67 | 3.89 | 3.00 | 2.33 | *3.18* | 20% |
| **BDS for SME digital transformation** | **3.11** | **2.91** | **3.59** | **3.51** | **3.53** | **3.33** | **10%** |
| *Design and implementation* | 3.22 | 3.04 | 3.51 | 3.47 | 3.51 | 3.35 | 70% |
| *Monitoring and evaluation* | 2.85 | 2.60 | 3.76 | 3.60 | 3.58 | 3.28 | 30% |
| **Outcome-oriented indicators** | **1.40** | **1.80** | **4.20** | **1.80** | **3.00** | **2.44** | **10%** |
| **Innovation policy for SMEs** | **3.00** | **2.85** | **3.44** | **3.11** | **3.03** | **3.09** | |
| **Policy framework for innovation** | **3.06** | **3.11** | **3.50** | **2.99** | **2.72** | **3.07** | **40%** |
| *Planning and design* | 3.56 | 3.03 | 3.08 | 3.13 | 3.40 | 3.24 | 35% |
| *Implementation* | 3.27 | 3.58 | 3.93 | 3.04 | 2.47 | 3.26 | 45% |
| *Monitoring and evaluation* | 1.70 | 2.20 | 3.25 | 2.60 | 2.10 | 2.37 | 20% |
| **Government institutional support** | **2.77** | **2.88** | **3.26** | **3.33** | **3.11** | **3.07** | **25%** |
| *Planning and design* | 3.00 | 3.00 | 3.70 | 3.70 | 3.30 | 3.34 | 35% |
| *Implementation* | 3.08 | 3.17 | 3.33 | 3.33 | 3.00 | 3.18 | 45% |
| *Monitoring and evaluation* | 1.67 | 2.00 | 2.33 | 2.67 | 3.00 | 2.33 | 20% |
| **Government financial support** | **3.62** | **2.82** | **3.56** | **3.28** | **2.67** | **3.19** | **25%** |
| *Planning and design* | 3.55 | 3.00 | 3.55 | 3.55 | 3.18 | 3.36 | 35% |
| *Implementation* | 3.86 | 3.00 | 3.86 | 3.29 | 2.71 | 3.34 | 45% |
| *Monitoring and evaluation* | 3.22 | 2.11 | 2.91 | 2.78 | 1.67 | 2.54 | 20% |
| **Outcome-oriented indicators** | **1.80** | **1.80** | **3.40** | **2.60** | **5.00** | **2.92** | **10%** |
| **Green economy policies for SMEs** | **2.51** | **2.54** | **3.08** | **3.38** | **2.56** | **2.81** | |
| **Environmental policies** | **2.89** | **2.82** | **3.57** | **3.70** | **2.44** | **3.08** | **35%** |
| *Planning and design* | 3.00 | 3.00 | 4.32 | 3.40 | 3.62 | 3.47 | 35% |
| *Implementation* | 3.00 | 3.16 | 3.16 | 4.00 | 1.83 | 3.03 | 45% |
| *Monitoring and evaluation* | 2.45 | 1.73 | 3.18 | 3.55 | 1.73 | 2.53 | 20% |
| **Incentives and instruments** | **2.54** | **2.40** | **3.14** | **3.60** | **2.92** | **2.92** | **55%** |
| *Planning and design* | 3.61 | 2.39 | 3.50 | 4.39 | 3.55 | 3.49 | 35% |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | Weight |
|---|---|---|---|---|---|---|---|
| *Implementation* | 2.39 | 2.58 | 3.36 | 2.82 | 2.85 | 2.80 | 45% |
| *Monitoring and evaluation* | 1.00 | 2.00 | 2.00 | 4.00 | 2.00 | 2.20 | 20% |
| **Outcome-oriented indicators** | **1.00** | **2.33** | **1.00** | **1.00** | **1.00** | **1.27** | **10%** |

Note: Dimension scores are presented based on the five levels of policy reform (see Table 2.21). Methodological changes have been introduced to the 2024 assessment based on lessons learnt from previous SBA assessments and to capture important changes and emerging trends in the business and policy environment. For more information about the scoring methodology, please refer to Annex A.

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## Notes

[1] These documents are listed and detailed in the Ukraine country profile.

[2] The ITU has set an international affordability target of 2% of GNI, at or below which an internet connection is deemed affordable.

# 3 Economic context

## Russia's invasion of Ukraine affects economic development in the EaP region

### *EaP countries hit by multiple shocks*

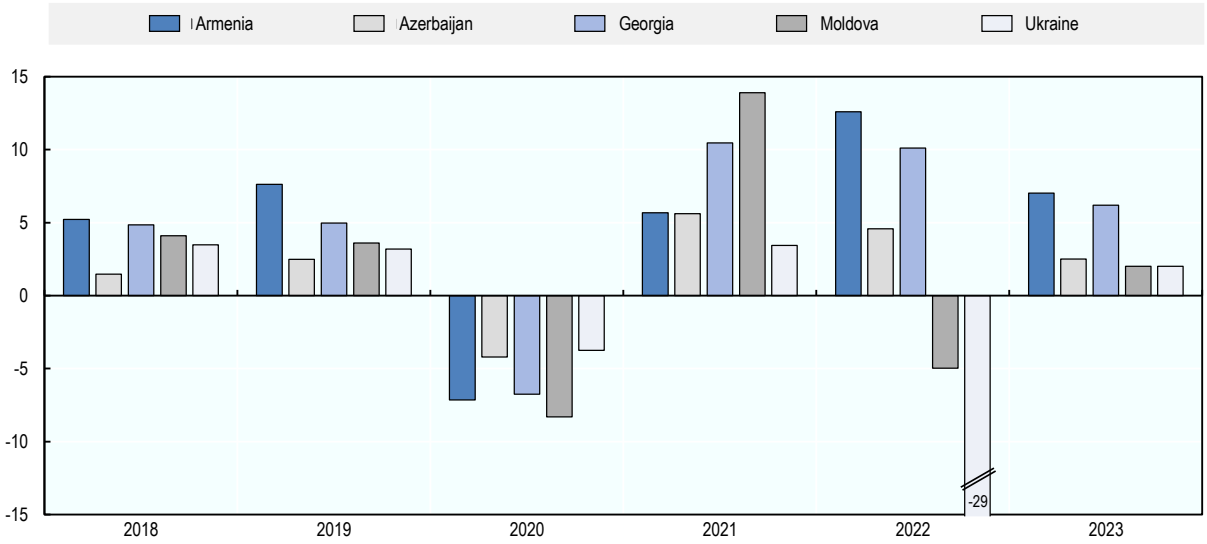
The four years since the previous SBA assessment have been marked by major socioeconomic and geopolitical shocks, above all the COVID-19 pandemic and Russia's war of aggression against Ukraine.

The outbreak of the COVID-19 pandemic in early 2020 caused an unprecedented health crisis for all countries around the world, with a spike in mortality due to COVID-19 estimated at close to 25 million excess deaths as of late July 2023, 320 000 of which occurred in EaP countries[1] (The Economist, 2023[1]). Governments across the world issued stay-at-home orders and restricted mobility, social interactions and economic activities to contain the spread of the virus, especially until effective vaccines became widely available in late 2020. To combat the pandemic and minimise its impact on households and businesses, governments also rolled out large fiscal stimulus measures, equivalent to over 15% of GDP for advanced economies and in the range of 1.4% to 7.1% for EaP countries[2] (IMF, 2021[2]).

The pandemic led to the sharpest economic contraction in the world economy (-3.1%) since World War II (Bolt and van Zanden, 2020[3]) (IMF, 2023[4]). EaP countries were no exception, with a large reduction in output due to the slowdown in economic activity and the restrictive measures introduced to contain the pandemic. The contraction was most pronounced in Armenia and Georgia, where the services sector, and tourism in particular, plays a relatively more important role; and in Moldova, where the pandemic's impact on the economy was made worse by one of the most severe droughts of the past two decades, causing cereal production to drop to half of its previous five-year average value (FAO, 2021[5]).

In 2021, the relaxation of COVID-19 restrictions and the resumption of international tourism, trade and investment flows sustained an economic rebound across the EaP region; GDP growth reached double digits in Georgia and Moldova, buoyed in particular by an increase in private consumption, public investment and exports in case of the former, and record-high cereal production in case of the latter (Figure 3.1).

## Figure 3.1. Annual percentage change in GDP growth in EaP countries (2018-23)




Note: 2022 and 2023 are estimates.
Source: (IMF, 2023[4]).

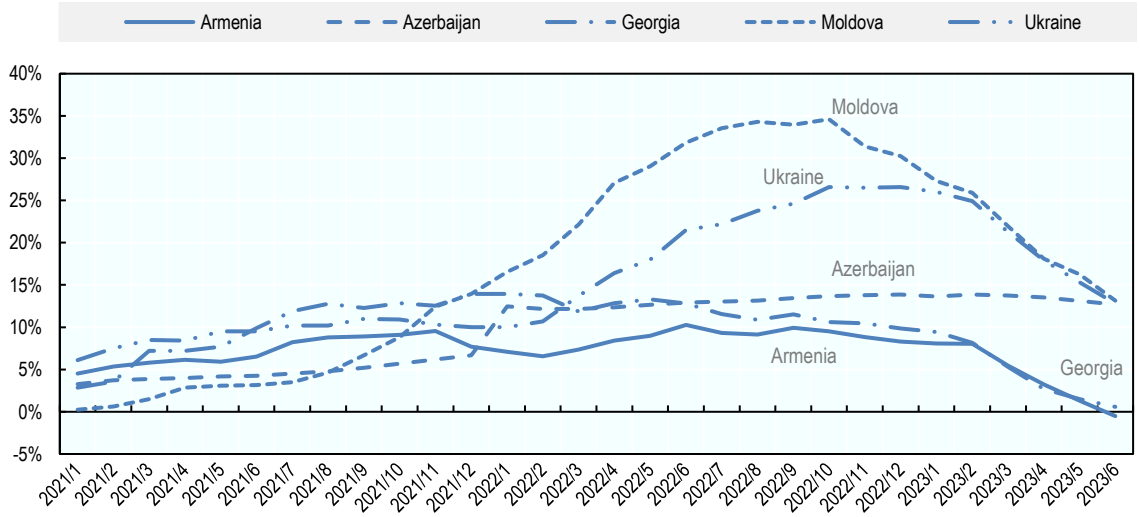
StatLink https://stat.link/610s57

The war in Ukraine put the EaP region at the epicentre of another global shock in February 2022, which caused a significant slowdown in global growth and severely challenged the trajectory of economic recovery in EaP countries. In addition to the human and economic tragedy for the Ukrainian people, the economic effects of the war reverberated across the entire world. Supply chains were disrupted as a result of export bans, the threat to shipping in the Black Sea, and international sanctions, all of which made it harder to get goods in and out of Russia and Ukraine. Because the two countries play a key role in the global supply of food and energy, this caused huge volatility in commodity markets, with prices of essential grains, energy and metals increasing dramatically after the invasion began (OECD, 2023[6]).

This exacerbated pre-existing inflationary pressures across the EaP region, with annual consumer price increases reaching double digits for all countries and peaking at 35% in the case of Moldova in late 2022 (Figure 3.2). On average, households across the EaP region allocate 59% of their total expenditure to basic goods[3] (vs. 39% in the EU), so an increase in the price of these goods can seriously affect their purchasing power, with a disproportionate impact on the lowest income groups (Eurostat, 2023[7]) (OECD, 2023[6]). Governments and central banks in the EaP region reacted with appropriate fiscal policy and successive rounds of monetary tightening, which helped bring inflation back to pre-war levels – and, in the case of Armenia and Georgia, below the national target rates – by mid-2023.

## Figure 3.2. Inflation in EaP countries (2021-23)

Annual inflation (CPI percentage change over corresponding month of previous year)




Note: CPI = consumer price index.
Source: Central banks of EaP countries.

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### *The heterogeneous impact of the war on EaP countries*

While all EaP countries have dealt with the global consequences of Russia's invasion of Ukraine, macroeconomic performance at the country level has largely reflected country-specific factors, such as their proximity to the belligerent countries, trade flows, migration patterns and resource endowments.

First and foremost, for Ukraine the war represents a human tragedy on a scale not seen in decades in Europe, with tens of thousands dying and millions of refugees escaping or being internally displaced (OHCHR, 2023[8]) (UNHCR, 2023[9]). Ukraine's productive capacity and trade relations have been devastated, causing GDP to fall by around 29% in 2022. In the first months of the war, manufacturing in the south and in the east completely stopped or was drastically reduced, and agricultural production was severely compromised due to destruction of farmland, limited availability of fertiliser and reallocation of labour from agriculture to the war effort. In 2022, the volume of exports of goods and services from Ukraine dropped by around 43%, while imports declined by 28% compared to 2021, owing to reduced output and blocked transport routes (IMF, 2023[4]). The direct damage to physical infrastructure amounted to nearly USD 150 billion as of April 2023 (KSE, 2023[10]), and some estimates suggest it will take at least a decade for the Ukrainian economy to recover to pre-war levels (EIU, 2022[11]).

Direct spillovers from the war heavily affected Moldova's economy, which in 2022 contracted by 5.6%. Soaring energy prices raised input costs for manufacturers, and high inflation challenged investment and economic growth. External trade initially suffered from sluggish growth in Moldova's EU trading partners and major disruptions, in particular Russia's blockade of Ukrainian ports on the Black Sea (only partially offset by the Black Sea Grain Initiative[4]). Furthermore, proximity to Ukraine meant that in the first months of the war Moldova faced the extra challenge of welcoming and providing assistance to a large inflow of refugees from Ukraine – more than 115 000 as of July 2023, making Moldova the largest receiver of Ukrainian refugees as a proportion of domestic population. This has put additional stress on the country's administrative machine and public finances (UNHCR, 2023[9]).

By contrast, defying initial forecasts, economies in the South Caucasus performed better than expected in 2022. In the case of Azerbaijan, where hydrocarbons typically account for over 90% of exports, high energy prices and increases in global oil demand boosted export receipts and pushed economic growth to 4.6%. The EU's desire to step up gas imports from Azerbaijan (in its efforts to reduce its dependence on Russian hydrocarbons) will also create an opportunity for more investment in the country's energy sector – although its reliance on hydrocarbons poses risks to long-term growth due to declining oil production, oil price volatility and the global transition away from fossil fuels (EC, 2022[12]). Recently, however, a rebound of private consumption to pre-pandemic levels and an increase in public investment should support economic growth (IMF, 2023[4]).

Armenia and Georgia experienced an even larger positive macroeconomic shock in 2022, with GDP growing by 12.6% and 10.1%, respectively (IMF, 2023[4]). Both countries received a significant influx of people relocating from Russia (primarily) and Belarus, concentrated in two key periods: immediately after the start of the war and during the wave of military mobilisation in Russia in the fall of 2022. By the end of 2022, it is estimated that approximately 55 000 Russian citizens had moved to Armenia and 100 000 Russian and Belarusian citizens had moved to Georgia, corresponding to 1.8% and 2.5% of the local populations, respectively (GET, 2023[13]). Primarily employed in the IT sector and earning above-average salaries, this new type of migrants provided a short-term boost to domestic consumption, in particular in the services and construction sector, and contributed to a substantial inflow of capital as they transferred their savings to their new countries of residence. Net exports for both Armenia and Georgia, boosted by increased demand from their main trading partners (e.g. China, Bulgaria) and high commodity prices (e.g. copper), contributed to strong local currency appreciation in both countries and in turn helped to keep imported inflationary pressure under control compared to other EaP countries (Figure 3.2).

### Box 3.1. New migration patterns in the South Caucasus

The effects of international sanctions, fear of political turmoil, the risk of conscription and a deterioration in economic conditions and prospects at home are prompting many Russian citizens to move to Armenia and Georgia. Between the start of the war and the end of 2022, approximately 100 000 Russians and Belarussians relocated to Georgia and 55 000 to Armenia, respectively. Most of them have settled in the capitals, Tbilisi and Yerevan. While it is not yet possible to determine how "permanent" these relocations will be, surveys suggest that the latter show a more long-term perspective to stay in Armenia in comparison to staying in Georgia. This might be driven by the high number of ethnic Armenians living in Russia.

A significant proportion of these emigrants seem to have entrepreneurial ambitions, with many working in the IT sector, as this is a more mobile industry and thus offers an easier option to work internationally. Nevertheless, local employers are also benefitting from the influx of skilled workers. Especially in Armenia, relocated Russians are often employed in local companies.

EaP countries have an opportunity to capitalise on this inflow of human capital and technological skill. Armenia and Georgia, which already have growing IT sectors, could bolster their tech industries and diffuse more digital knowledge into their labour market. The creation of new IT companies in the two countries could also provide additional services for firms looking to digitalise, thereby assisting with broader ambitions for digitalisation in the EaP region.

Source: (OECD, 2023[6]); (GET, 2023[13]).

Despite the mixed results outlined above, important vulnerabilities remain for all economies in the EaP region, related to both the evolution of the war in Ukraine and its local and global consequences (described below) but also to each country's long-term structural issues (described in the next section).

While Ukraine has demonstrated strong signs of economic resilience (e.g. the relocation of businesses to safer parts of the country, an advanced and growing IT sector, the establishment of new export routes), the socio-economic outlook for the country will remain highly uncertain as long as the war continues and until the reconstruction effort can take place undeterred by the constant threat of military attack.

For the other EaP countries, long-standing commercial and financial ties with the economies of Russia and Ukraine, both experiencing the worst recession seen in decades, represent a source of potential vulnerability (via a reduction in exports, investment and remittances) that can only partially be offset in the short-term with product and market diversification efforts, especially for the sectors traditionally most exposed to Russian demand (e.g. wine, spirits, ferro-silico-manganese). This is in addition to each country's specific exposure to the renewed risks of high global prices of energy and food commodities, as all EaP countries are net importers of energy (except Azerbaijan) and rely heavily on imports of wheat (except Moldova), a key food staple in the region, from Russia and Ukraine (OECD, 2023[6]).

Specifically for the countries in the South Caucasus, the positive macroeconomic trends described earlier are likely to be driven by one-off factors which may reverse or at least fade out in the near term. For Azerbaijan's economy, exposure to oil price volatility represents a source of uncertainty which should incentivise the country to diversify its productive structure and look for alternative sources of growth. For Armenia and Georgia, the inflow of Russian citizens, which in 2022 propelled the two economies to double-digit growth, is very unlikely to continue at the same pace in the coming years. On the contrary, while it appears that many have moved to the two countries with the intention of staying at least in the medium term, there is a possibility that a substantial share may decide to return to Russia if conditions at home improve or to move on to a third country if their prospects in Armenia and Georgia do not meet their expectations.

## A diverse region with an evolving economic structure

EaP countries are well located to facilitate engagement with important economic partners. While Moldova and Ukraine both share a border with the EU, the South Caucasus is an important transit region for the Middle Corridor connecting Central Asia with Europe. Nevertheless, the EaP region is heterogeneous, with great variation in population, land size, and natural resource endowments. These differences influence each country's economic structure as well as determine their evolution.

## Box 3.2. Economic Snapshots

### Armenia

Armenia, a landlocked and mountainous country, is the smallest of the five EaP countries. Its economy is driven mainly by the service sector, which accounted for 55.3% of the value added in 2022. The most exported goods are ores, slag and ash, with a collective share of 30% of total exports. However, the overall trade balance is negative. Exports to Russia have been increasing slowly but steadily and have exceeded exports to the EU since 2019. The country also has the highest inward direct investment from Russia as well as the lowest from the EU among the five EaP countries (IMF, 2021[14]). The share of SMEs has been constantly rising in the economy and now makes up 99.85%. Their value added shows the same trend but remains much lower due to a prevailing productivity gap in comparison to large enterprises.

### Azerbaijan

Azerbaijan's economy is dominated by mining and quarrying activities, which accounted for 45% of the value added in 2022. The oil and gas industry plays an especially important role, as Azerbaijan produces substantially more energy than it consumes (IEA, 2021[15]). As a result, most of its oil and gas is exported, accounting for around 92% of export revenues in 2022 and contributing to a large positive trade balance (Ministry of Energy of the Republic of Azerbaijan, 2023[16]). SMEs' contribution to the economy is the lowest among EaP countries even though they account for 99.7% of enterprises. Consequently, Azerbaijan also has the largest productivity gap between SMEs and large enterprises.

### Georgia

Georgia's economy has the biggest value added of the service sector among all five EaP countries, with almost 60% in 2022. Exports to the EU decreased in 2020 due to the pandemic but rebounded to pre-pandemic levels in 2022, with the single market representing the first export destination for Georgian products. Exports to Russia have also rebounded to above pre-pandemic levels but remain substantially lower than to the EU. The country's large infrastructure project on the Anaklia Deep Sea Port was revived in December 2022 after being put on hold for almost two years (Dzamukashvili, 2023[17]). Upon completion, it is expected to turn Georgia into a logistics and transport hub promoting the Middle Corridor and offering an alternative to the transport route through Russia. SMEs' contribution to the economy has remained rather stable relative to larger firms in recent years.

### Moldova

Moldova exhibits the highest share of rural population among the EaP countries (56%). It is also heavily reliant on the exports of agricultural products, with Russia being an important partner. GDP growth suffered from the consequences of the war in Ukraine (-5.6% in 2022), although in 2021 it had grown strongly (13.9%) after declining by 8% the year before. In general, Moldova's economy is historically highly dependent on personal remittances, equivalent to 14% of GDP in 2022. Stability remains at risk due to Russia's war of aggression in neighbouring Ukraine. Inflation levels in Moldova have continuously been the highest among the EaP countries since the beginning of 2022, peaking at 35%. Moldova's share of SMEs was at 98% in 2021, but their contribution to the economy is slowly decreasing.

### Ukraine

Ukraine's economy has been severely damaged by Russia's military aggression, which caused GDP to shrink by 29% and inflation to surge to 26% in 2022. It is the largest economy among the EaP countries and receives the highest inward direct investment from the EU (32% of GDP in 2021) (IMF,

2021[14]). Russian direct investment, on the other hand, has been continuously low at around 1% in the past years. The country possesses 30% of the world's black soil, which is extremely fertile, giving its agricultural industry an important advantage. Thus, the primary sector accounted for 10.6% of value added in 2021 and cereals made up about 20% of the total export volume of Ukraine in the previous three years. However, due to Russia's invasion, both export volume and value added significantly declined in 2022. Before the war, SMEs' contribution in the economy showed an increasing trend and their share of value added was the highest among EaP countries in 2021.

Note: Data from World Development Indicators and National Statistical Offices unless indicated otherwise.

With the exception of Azerbaijan, the EaP countries have limited natural resource endowments. Moldova and Georgia exploit very low natural resource rents (less than 1.5% of GDP in 2021). By contrast, Armenia and Ukraine experienced a jump in such rents from less than 2.4% and 1.1% in 2020 to around 7.1% and 7.5%, respectively, in 2021. Azerbaijan, which is rich in oil and natural gas, has the highest natural resource rents among EaP countries, at almost 30% of GDP in 2021, owing to the jumps in the price of and global demand for energy that followed the global recession in 2020 (World Bank, n.d.[18]).

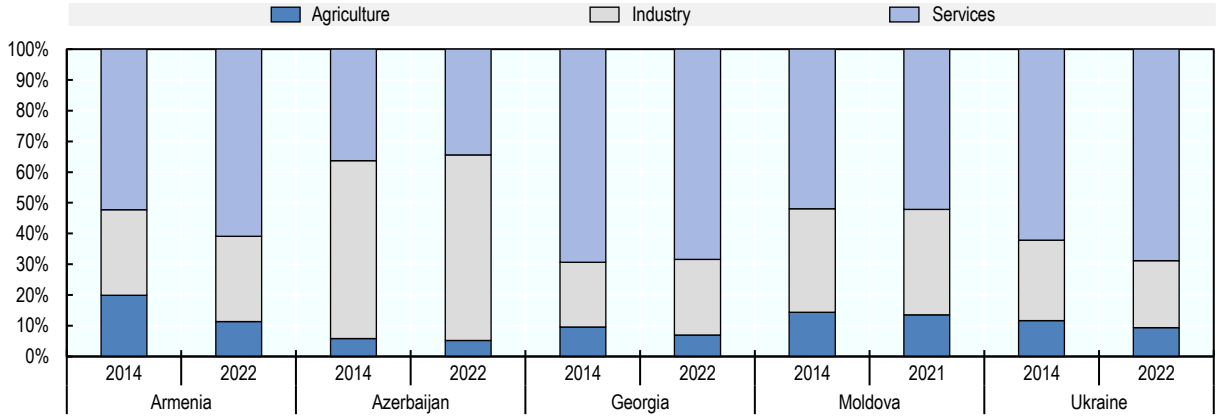
With the exception of Georgia, the share of arable land among EaP countries in 2021 is higher than the OECD average. In Moldova and Ukraine, arable land makes up more than half of the total territory due to a high endowment of extremely fertile black soil, which gives agricultural activity a competitive edge. Moldova also has a high share of rural population (56% in 2022), whereas rural dwellings in the other EaP countries constitute only between 30% and 43% of the population (World Bank, n.d.[18]). These are still significantly higher than the OECD or EU averages, with important implications for the design and implementation of national SME policies.

Rural areas face several disadvantages with respect to urban areas, especially when it comes to entrepreneurship. There is less access to young talent, skilled workers and financial resources. However, fostering entrepreneurship among rural populations can be an important source of job creation and a driver of formalisation of economic activities (European Regional Development Fund, 2020[19]).

With the exception of Moldova, all EaP countries are experiencing a declining share of agriculture in GDP (Figure 3.3). However, the contraction in Ukraine's agricultural sector stems mainly from the impact of the war. Conversely, the services sector is gaining importance in most countries and represents the biggest contributor to GDP across the EaP region, with the exception of Azerbaijan. Due to Azerbaijan's significant endowments of natural resources, industry still plays the most important role in the country, especially because global natural resource prices have risen and many countries are imposing sanctions on and diversifying away from Russia's supply of natural resources. The relatively large size of the service sectors in Armenia and Georgia also reflects the importance in their economies of tourism – which, despite being subject to a high degree of seasonality, has increased substantially in recent years (Geostat, 2023[20]).

## Figure 3.3. GDP composition in EaP countries

2014 compared to 2022



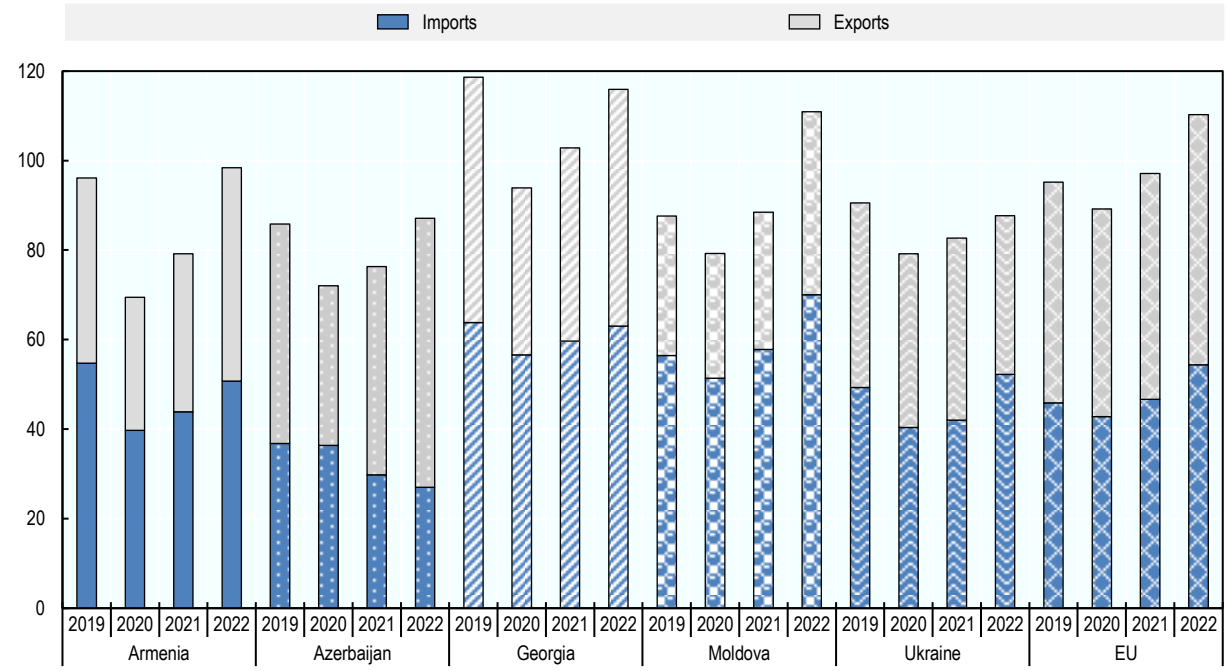

Note: According to International Standard of Industrial Classification (ISIC) classification.
Source: National Statistical Offices of EaP countries.

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EaP economies depend greatly on trade and thus are highly exposed to macroeconomic shocks. Most EaP countries run trade and current account deficits with the biggest negative trade balance in 2022 being recorded by Moldova, followed by Ukraine (Figure 3.4). In contrast, Azerbaijan has a high positive trade balance due to its hydrocarbon exports. Imports and exports in the EaP region were significantly affected by the COVID-19 pandemic, when border closures and restriction of movement caused the disruption of trade flows and supply chains (OECD, 2020[21]). Consequently, COVID-19 caused a contraction in trade openness (the sum of imports and exports as a percentage of GDP) of almost 20 percentage points on average in the EaP region in 2020. In 2021-22, imports and exports increased again surpassing pre-pandemic levels except in Ukraine. Due to the war, Ukrainian exports dropped sharply by 30% in comparison to 2021.

## Figure 3.4. Exports and imports in EaP countries and peers (% of GDP)

2019 to 2022




Source: World Development Indicators (World Bank, n.d.[18]).

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## Box 3.3. EaP countries and their shifting role in global value chains

Global value chains (GVCs) have emerged as a defining feature of the world economy over the last 40 years. The international organisation of production enabled by (ICTs), declining trade costs, the integration into world trade of emerging economies in eastern Europe and Asia, and the rise of multinational enterprises have all contributed to an increase in countries' participation in GVCs.

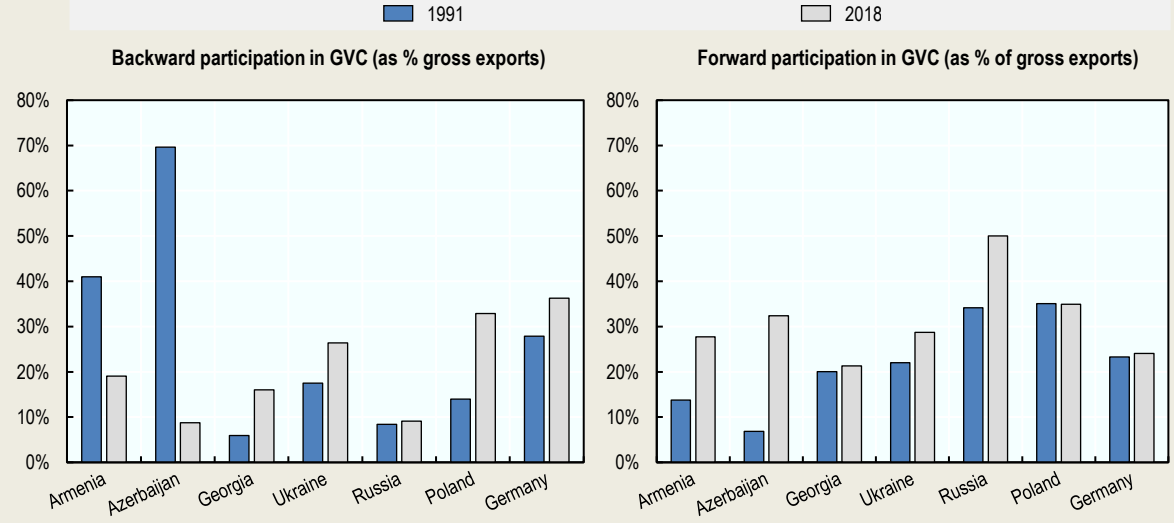
When production is fragmented across multiple countries and intermediate goods cross multiple borders before reaching consumers, traditional measures of gross exports can be subject to double counting. To address this issue, the international community of trade researchers has developed the concept of "trade in value added" in an effort to map GVCs and better reflect where value added is produced – effectively distinguishing in a country's exports the portion of value added created domestically from the portion of value added of foreign origin, imported as intermediate inputs.

Two indicators can thus be considered for the analysis of participation in GVCs:

- *Backward participation*: foreign value added embodied in a country's exports
- *Forward participation*: domestic value added of a country embodied in other countries' exports

Participation in GVCs enables countries to specialise in areas of comparative advantage, enhancing productivity growth and supporting wages and incomes. Over the last few decades, EaP countries have experienced significant shifts in their respective degrees of GVC participation, reflecting the changing structure of their economies (Figure 3.5).

### Figure 3.5. EaP countries' participation in GVCs




Source: OECD analysis based on UNCTAD-EORA GVC database (data for Moldova not available)

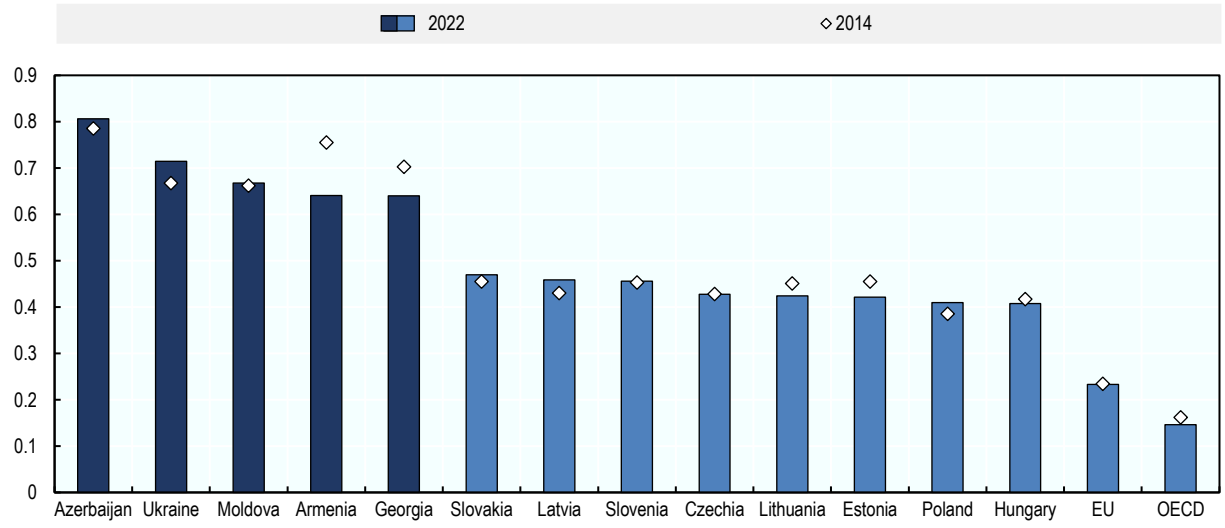
While increasing for Georgia and Ukraine, levels of backward participation in GVCs are still lower than in OECD economies such as Poland or Germany. This is partly due to the lesser sophistication of their exported manufacturing output, which requires foreign components as intermediate inputs. The low values of exports for Armenia and Azerbaijan in the early 1990s help to explain the evolution in both backward and forward linkages for the two countries: increasing exports of commodities extracted locally have reduced the relative contribution of foreign value added, while they have caused their forward participation to jump since energy and minerals (e.g., copper) serve as inputs in partner countries' production.

Source: (Cigna, Gunnella and Quaglietti, 2022[22]); (Casella et al., 2019[23]).

EaP economies are also vulnerable because of their limited product diversification (Figure 3.6). They are all characterized by a high concentration of exported products, which exposes them to volatile commodity prices. Since 2014, product diversification has increased in Armenia and Georgia but declined slightly in Azerbaijan, Moldova and Ukraine. The EU and OECD averages indicate highly diversified export baskets that differ significantly from the EaP average.

## Figure 3.6. Product diversification index in EaP countries and peers

2014 and 2022



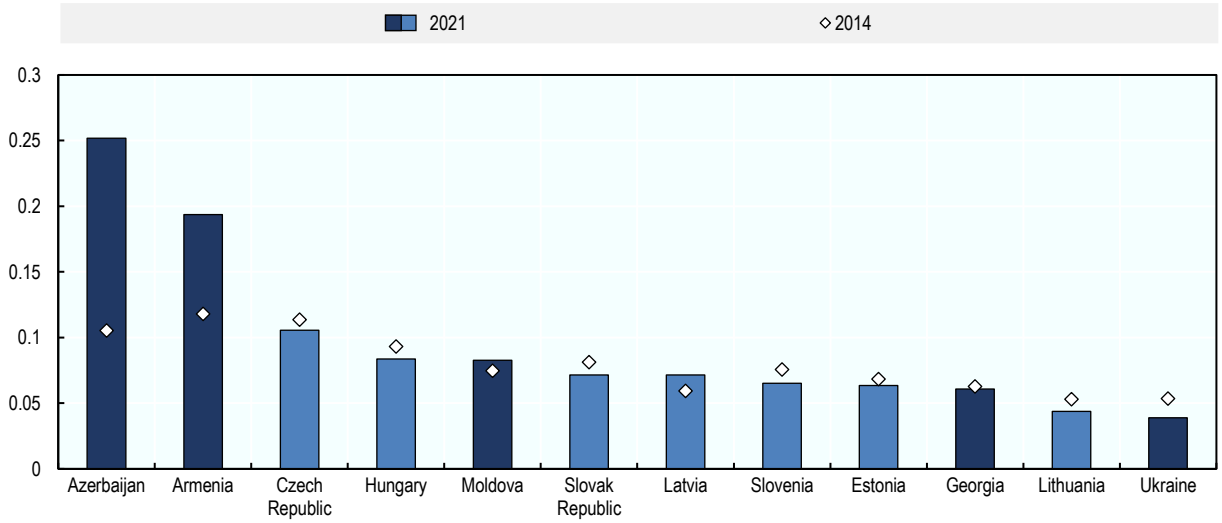

Note: The product diversification index is computed by measuring the absolute deviation of the trade structure of a country from the world structure. It takes values between 0 and 1; a value closer to 1 indicates a greater divergence from the world pattern.
Source: (UNCTAD, n.d.[24]).

StatLink https://stat.link/jtpxoy

When it comes to trade partners' market concentration, EaP countries are equally vulnerable. Markets are especially concentrated in Azerbaijan and Armenia, while Ukraine had the lowest indicator of market concentration in the EaP region and among regional peers in 2021 (Figure 3.7). In fact, all EaP countries except Ukraine and Georgia transitioned to higher levels of market concentration between 2014 and 2021, whereas almost all peers moved towards lower concentration. A less diversified set of trade partners exposes the economy to higher risks in case of macroeconomic shocks, as established bilateral supply chains cannot be redefined in the very short term.

## Figure 3.7. Market concentration in EaP countries and peers

Herfindahl Hirschman Index in 2014 and 2021




Note: The Herfindahl Hirschman index is a measure of dispersion of trade value across an exporter's partners. A country with trade (export or import) that is concentrated in a very few markets will have an index value close to 1. Similarly, a country with a perfectly diversified trade portfolio will have an index close to zero.
Source: (WITS, n.d.[25]).

StatLink https://stat.link/gipea7

With the exception of Ukraine, EaP countries still rely heavily on Russia as a trading partner. Armenia, in particular, exhibits a massive dependence, with 30% of imports and 45% of exports coming from, and going to, Russia (Table 3.1). In light of the current sanctions against Russia, as well as Russia's uncertain economic outlook, greater diversification of trade partners will reduce vulnerabilities of EaP economies. Goods exported from the EaP region are mainly raw materials. Whereas in the South Caucasus natural resources like copper ores, oil, and gas are important export goods, Eastern Europe focuses on agricultural goods. Motor cars (most of which are then re-exported) and refined oils consistently rank at the top of the list of goods imported by EaP countries (Table 3.1).

## Table 3.1. Structure of imports and exports in EaP countries in 2022

Top three imported and exported goods at HS-2 level

| | Top three imported goods | Main sources of imports | Top three exported goods | Main export destinations |
|---|---|---|---|---|
| Armenia | Motor cars and vehicles (7%)<br>Petroleum oils (7%)<br>Petroleum gases (6%) | Russia (30%)<br>China (15%)<br>Iran (7%) | Copper ores and concentrates (13%)<br>Gold (8%)<br>Diamonds (7%) | Russia (47%)<br>United Arab Emirates (10%)<br>China (7%) |
| Azerbaijan | Motor cars and vehicles (6%)<br>Petroleum oils (5%)<br>Medicaments (3%) | Russia (19%)<br>Türkiye (16%)<br>China (14%) | Crude oil (51%)<br>Gas (39%)<br>Refined oils (1%) | Italy (47%)<br>Türkiye (9%)<br>Israel (4%) |
| Georgia | Motor cars and vehicles (13%)<br>Petroleum oils (10%)<br>Copper ores and concentrates (6%) | Türkiye (18%)<br>Russia (14%)<br>China (8%) | Copper ores and concentrates (28%)<br>Ferroalloys (12%)<br>Fertilisers (8%) | China (19%)<br>Russia (14%)<br>Bulgaria (11%) |
| Moldova | Petroleum oils (16%)<br>Petroleum gases (9%)<br>Motor cars and vehicles (4%) | Romania (18%)<br>Russia (12%)<br>China (10%) | Insulated wire, cable and other electric conductors (14%)<br>Seed oils (12%) | Romania (34%)<br>Türkiye (8%)<br>Italy (6%) |

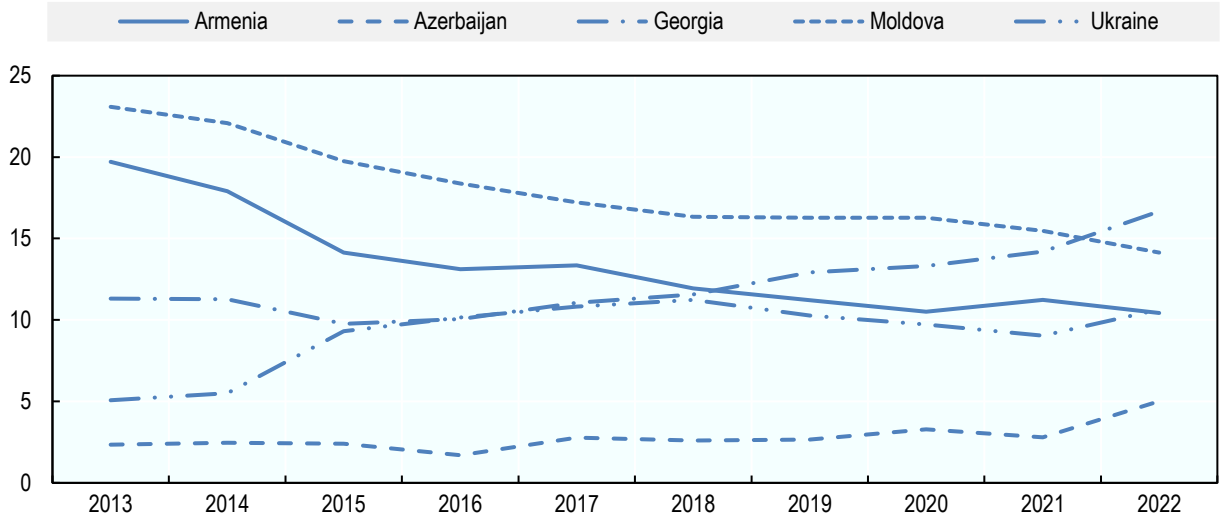
| | Top three imported goods | Main sources of imports | Top three exported goods | Main export destinations |
|---|---|---|---|---|
| | | | Maize (11%) | |
| Ukraine | Petroleum oils (16%)<br>Motor cars and vehicles (5%)<br>Unspecified commodities (4%) | China (16%)<br>Poland (10%)<br>Germany (8%) | Maize (13%)<br>Seed oils (12%)<br>Iron ores and concentrates (7%) | Poland (15%)<br>Romania (9%)<br>Türkiye (7%) |

Note: Table does not include trade in services. Exports refer to domestic exports except for Ukraine and Azerbaijan. Imports include re-imports.
Source: UN Comtrade Database.

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Remittance inflows remain high in most EaP countries. While they have been steadily rising in Georgia, which recorded the highest remittances received in 2022 (as share of GDP), a decreasing trend can be observed in Moldova and Armenia (Figure 3.8). Ukraine and Azerbaijan experienced a reversal of the decreasing trend in 2021-22, with a jump in remittance inflows of about 2 percentage points. As recent research shows, the high dependence on remittance income exposes EaP economies to potential shocks (e.g. economic contraction, currency depreciation) in the countries where labour migrants generate their income (Meduza, 2023[26])

## Figure 3.8. Personal remittances received in EaP countries (percentage of GDP)




Source: World Development Indicators (World Bank, n.d.[18]).

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### *Untapped potential of SMEs in EaP countries*

Competitive and diversified economies require a dynamic SME sector in order to seize emerging market opportunities, create new jobs and innovate. As such, SMEs and entrepreneurs also play a crucial role in the adaptation of societies to major global trends – including digitalisation, globalisation, demographic shifts, labour market transformations and the transition to more sustainable business practices.

At the same time, the SME and entrepreneur population is very diverse with respect to their size, sector, age, location, background, capacities and aspirations, as well as their ability to overcome inefficiencies in the business environment and policy sphere.

Across the EaP region, SMEs make up over 98% of total enterprises and between 60% and 80% of employment (except in Azerbaijan), while their contribution to value added is much smaller (Table 3.2).

### Table 3.2. Business demography indicators in EaP countries (2021 or latest available)

| | Armenia | | Azerbaijan | | Georgia | | Moldova | | Ukraine | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Number | Share | Number | Share | Number | Share | Number | Share | Number | Share |
| **Enterprises** | | | | | | | | | | |
| Micro | 85,150 | 94.7% | 346,171 | 97.0% | - | - | 51,335 | 85.1% | 1,880,858 | 96.1% |
| Small | 3,994 | 4.4% | 6,856 | 1.9% | 201,582 | 98.2% | 6,579 | 10.9% | 56,969 | 2.9% |
| Medium | 687 | 0.8% | 2,879 | 0.8% | 3,033 | 1.5% | 1,443 | 2.4% | 17,811 | 0.9% |
| Large | 133 | 0.15% | 1.059 | 0.3% | 655 | 0.3% | 965 | 1.6% | 610 | 0.03% |
| SMEs | 89,831 | 99.9% | 355,906 | 99.7% | 205,270 | 99.7% | 59,357 | 98.4% | 1,955,638 | 99.9% |
| **Employment** | | | | | | | | | | |
| Micro | 96,837 | 28.0% | 40,909 | 4.8% | - | - | 104,703 | 19.7% | 3,127,387 | 35.0% |
| Small | 74,712 | 21.6% | 102,180 | 11.9% | 313,125 | 42.1% | 114,369 | 21.5% | 1,160,337 | 13.0% |
| Medium | 69,107 | 19.9% | 214,751 | 25.1% | 146,950 | 19.7% | 95,853 | 18.0% | 2,999,712 | 33.6% |
| Large | 105,231 | 30.4% | 499, 328 | 58.2% | 284,181 | 38.2% | 217,943 | 40.9% | 1,648,692 | 18.4% |
| SMEs | 240,656 | 69.6% | 357,840 | 41.8% | 460,075 | 61.8% | 314,925 | 59.2% | 7,287,436 | 81.6% |
| **Value added (local currency)** | | | | | | | | | | |
| Micro | 787,702 | 25.8% | 5,791 | 6.8% | - | - | 50,106 | 10.3% | - | 18.7% |
| Small | 556,638 | 18.3% | 2,384 | 2.8% | 8,050 | 28.90% | 76,340 | 15.6% | - | 15.0% |
| Medium | 588,105 | 19.3% | 5,781 | 6.8% | 6,641 | 23.9% | 57,124 | 11.7% | - | 36.5% |
| Large | 1,115,312 | 36.6% | - | 83.6% | 13,153 | 47.2% | 304,648 | 62.4% | - | 29.8% |
| SMEs | 1,932,444 | 63.4% | 13,956 | 16.4% | 14,691 | 52.8% | 183,570 | 37.6% | - | 70.2% |

Note: Value added for Ukraine refers to 2020. Moldova's value added reflects turnover. Percentages may not sum to 100% due to rounding.
Source: National Statistical Offices.

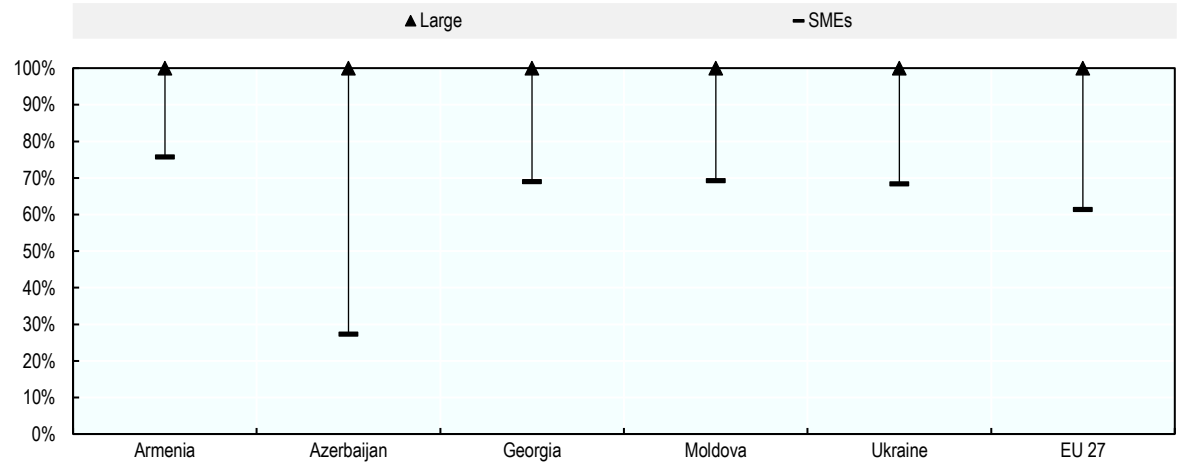
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Despite the high share of SMEs in EaP economies, they still exhibit a significant productivity gap in comparison to large firms (Figure 3.9). This is unsurprising – not only because capital-intensive manufacturing generates increasing return to scale, but also because (i) SMEs in the EaP region are concentrated in low-value-added services sectors (wholesale and retail trade); and (ii) the professional, scientific and technical activities (legal and consulting services) in which SMEs can outperform larger firms in more advanced economies are still at a very nascent stage.

Allowing entrepreneurs to take risks, easily start new business ventures, grow and better integrate into global value chains would result in greater diversification, higher-quality job creation, and ultimately a more modern and productive SME sector in EaP countries.

## Figure 3.9. SME productivity gap

Value added per person employed, as share of large enterprises, 2021




Note: Productivity is measured by value added per person employed. For Moldova, "Profits before taxation" were used because data on value added are not available. Data for Ukraine are from 2020.
Source: Statistical offices of EaP countries

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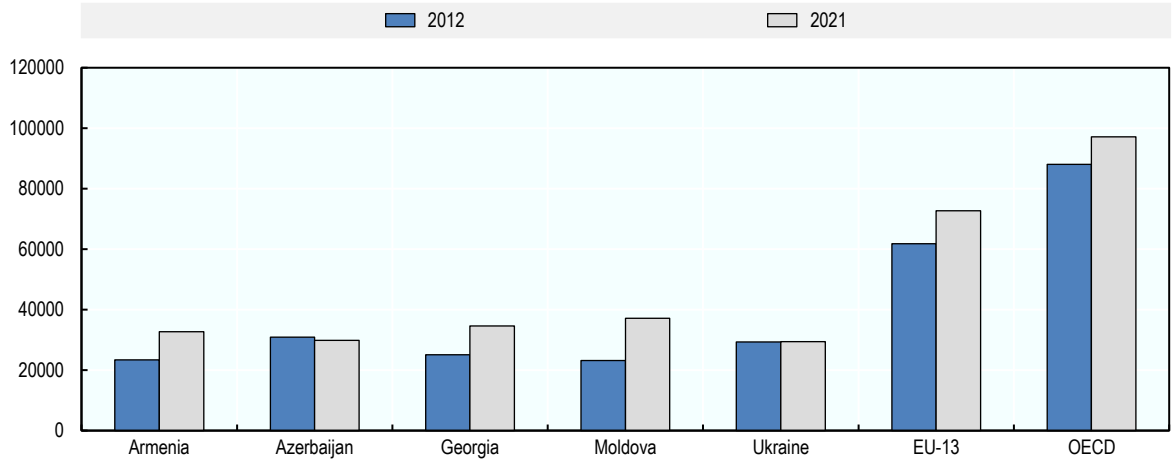
## Digitalisation as a strategic policy priority to modernise EaP economies

EaP countries' efforts to modernise their emerging economies represent a long-term process that will require implementing a wide range of structural reforms. These include building and maintaining a competitive environment, investing in education for a skilled labour force, and fostering private entrepreneurship and innovation so that firms can engage in higher value-added activities and manufacture higher-complexity products to diversify exports.

While progressing at different speeds, EaP countries have come a long way since their regained independence after the fall of the Soviet Union. In relative terms, sizeable improvements have occurred in the last decade – in particular in Armenia, Georgia and Moldova (Figure 3.10). However, overall productivity levels remain far below those of EU-13 and OECD Members.

## Figure 3.10. Labour productivity in EaP, EU-13 and OECD (2012-21)

Output per worker, constant 2017 international $ at PPP




Note: EU-13 refers to Bulgaria, Croatia, Cyprus, Czechia, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, the Slovak Republic and Slovenia.
Source: (International Labour Organization, n.d.[27]).

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In this low-productivity context, the adoption of both established digital tools and emerging digital technologies[5] represents an opportunity for businesses in EaP countries to transform the way they produce goods and services, innovate and interact with other firms, workers, consumers and governments. This "digital transformation" can bring a wide range of benefits to a company's operations and, ultimately, promises a vast potential to enhance firm productivity.

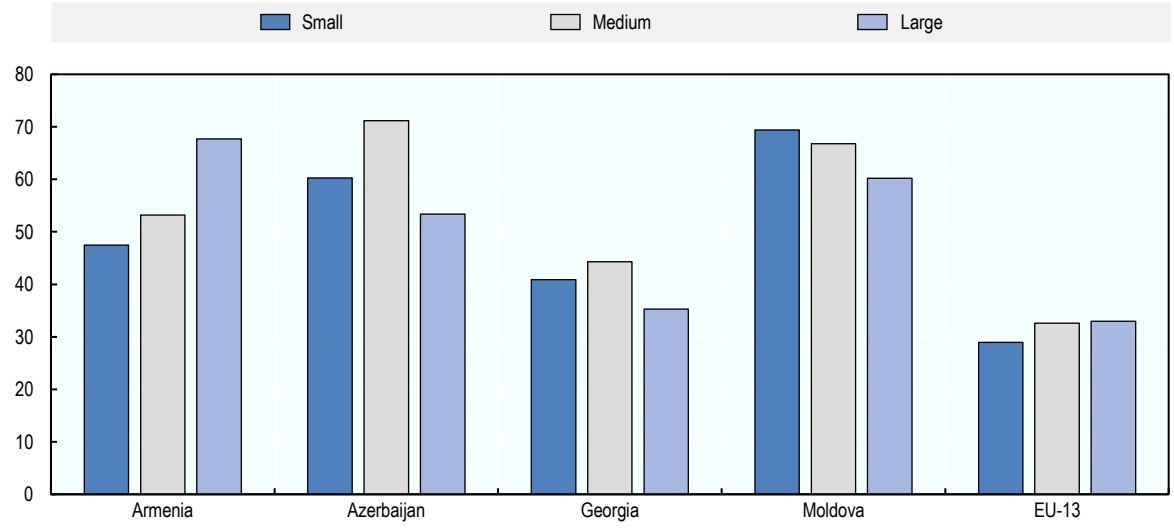
While the full impact on productivity of emerging "general purpose" technologies such as artificial intelligence has yet to materialise, the literature has already described the existence of positive links between the adoption of established digital tools and firm productivity. For example, one recent estimate based on firm-level data from EU countries suggests that a 10-percentage-point increase in the share of firms using cloud computing in a given industry is associated with a 2.3% increase in productivity for the average firm in the same industry after three years (Gal, Nicoletti and Timiliotis, 2019[28]).

For SMEs, in particular, increased digitalisation represents a necessary condition to prevent the productivity gap with large enterprises from widening. Diffusion rates of digital technologies are consistently lower among SMEs compared to large firms across all technologies for which data are available; even within the SME sector, smaller firms have a lower likelihood of adopting digital tools than medium-size ones (OECD, 2021[29]).

However, three trends suggest that the time is ripe for embracing the digital transformation of SMEs as a strategic policy priority for EaP countries. First, the COVID-19 pandemic pushed many firms online for the first time, in many cases as a necessary measure to continue business operations. A large proportion of SMEs experienced first-hand the value of online marketing, e-commerce and remote working – and thus discovered new ways of doing business which have now been integrated into their operations in the post-pandemic environment (Figure 3.11).

## Figure 3.11. Increased digitalisation during the COVID-19 pandemic

Percentage of firms that started or increased online business activity in response to COVID-19



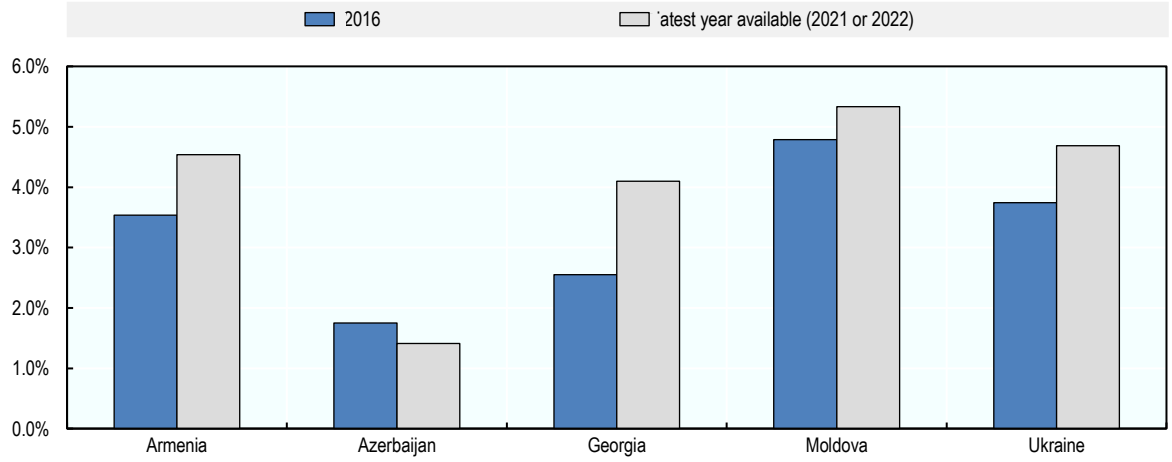

Note: EU-13 refers to Bulgaria, Croatia, Cyprus, Czechia, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, the Slovak Republic and Slovenia.
Source: World Bank Enterprise Survey (World Bank, n.d.[30]).

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Second, the ICT industry has been expanding quickly in most EaP countries, contributing to the growth of the higher value-added services sector and export diversification (Figure 3.12). A growing pool of IT professionals not only can supply locally-developed digital solutions for SMEs in EaP countries, but also represents an important resource for SME managers looking to recruit skilled human capital who can drive the digital transformation from within the firm.

## Figure 3.12. Growing relevance of ICT sector in EaP economies

Share of information and communication economic activities in country's GDP, from 2016 to the latest year available




Note: Data shown correspond to section J of the NACE Rev.2 classification of economic activities, which includes publishing activities; motion picture, video and television programme production; sound recording and music publishing activities; programming and broadcasting activities; telecommunications; computer programming; consultancy and related activities; and information service activities. Latest year available is 2021 for Moldova and Ukraine and 2022 for Armenia, Azerbaijan and Georgia.
Source: National Statistical Offices of EaP countries.

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Third, EaP countries have already made great strides in digitalising their government services, leveraging existing and emerging digital technologies to improve the quality, efficiency and effectiveness of the services they provide to citizens and businesses. Specifically for businesses, dedicated platforms have been set up to help SMEs and entrepreneurs liaise with the public administration and cut red tape. These "single digital portals" or "digital one-stop shops" serve as single entry points for accessing digital government services, reducing redundancy in public administration requests (OECD, forthcoming[31]). As documented in several parts of this report, all EaP countries have advanced in this area – in some cases, such as Ukraine's Diia e-government ecosystem, setting new global standards and inspiring other governments to rethink how they digitalise their services (USAID, 2023[32]).

Altogether, the trends presented above describe a fertile environment in EaP countries for increasing the digitalisation of the private sector, and of SMEs in particular. To achieve this, policy makers should adopt a comprehensive approach to designing and implementing policies for SME digitalisation, starting with a continuous improvement of the broad "framework conditions" enabling the digital transformation of economies and societies (e.g., broadband infrastructure, national digital strategies, digital skills). Further, governments should reflect on the widespread impact of digitalisation on the many facets of SME policy, staying up-to-date with technological developments and mainstreaming digitalisation concerns and opportunities in all policy dimensions. Lastly, it will be important to directly address the needs of SMEs by designing specific support programmes to stimulate SMEs' digital transformation.

The updated methodology underpinning this edition of the SME Policy Index aims to incorporate the progress made by EaP governments in supporting the digital transformation of SMEs as part of its broader assessment. As such, it will serve as a reference to continuously improve national SME policies, incorporating analysis and best practices focused on policy approaches and instruments supporting SME digitalisation. The results of the assessment and its recommendations are presented in the following chapters.

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## Notes

[1] The standard method of tracking changes in total mortality is “excess deaths”. This number is the gap between how many people died in a given region during a given time period, regardless of cause, and how many deaths would have been expected if a particular circumstance (such as a natural disaster or disease outbreak) had not occurred.

[2] Key fiscal measures announced or taken by governments in response to the COVID-19 pandemic as of 27 September 2021.

[3] Defined as food; housing; water; electricity; and gas and other fuels.

[4] Designated to counter the rise in world food prices and the threat of famine in lower-income countries, the Black Sea Grain Initiative is a UN-brokered agreement between Türkiye, the Russian Federation and Ukraine to safely export grain and fertilizer from three key Ukrainian ports in the Black Sea – Odesa, Chornomorsk and Yuzhny/Pivdennyi. While the Initiative allowed the safe export of nearly 33 million tonnes of grain and foodstuffs to 45 countries by over 1 000 vessels from July 2022 to July 2023, at the time of writing, the Initiative had not been renewed after its third term, which expired on 17 July 2023.

[5] Examples of “established” digital technologies, with proven applications and known value for businesses, are enterprise resource planning systems, customer relationship management and supply-chain management software, social media, e-commerce and electronic invoicing. Examples of “emerging” digital technologies underpinning the fourth industrial revolution are: 5G connectivity, the Internet of Things, big-data analytics, cloud computing and artificial intelligence. (OECD, 2021[29])

# Part I. Assessment findings by pillar

# 4 Digital Economy for SMEs

While digitalisation has proven to be a tool for resilience, notably during the COVID-19 crisis, SMEs still have not fully tapped into its potential. The 2024 SBA assessment therefore introduces a new section dedicated to the digital transformation of SMEs. This chapter measures EaP countries' progress in supporting SME digitalisation, looking at 1) selected framework conditions for the digital transformation – policy frameworks, such as national digital strategies; broadband connectivity; and digital skills – and 2) specific policy instruments to support SME digitalisation. It presents resulting composite scores for SME digitalisation policies. It depicts the region's advancement regarding the selected framework conditions, formulating recommendations for each of these aspects to address remaining challenges and bridge digital divides. In addition, this chapter summarises of the key findings reported for digitalisation-oriented sub-dimensions across other thematic chapters, assessing the presence and implementation of instruments that support SME digitalisation in all five EaP countries.

## Introduction

The process of digitalisation and the digital economy are closely intertwined, as they work in synergy, driving each other's growth. Digitalisation involves "the use of digital technologies, data and interconnectedness that result in new activities or existing ones" (OECD, 2021[1]). Adopting digital technologies enables companies to operate more efficiently, reach wider audiences, and offer more innovative digital products and services, fuelling the growth of the digital economy (OECD, 2022[2]). In turn, the digital economy accelerates digitalisation by creating the right incentives for businesses to further embrace digital technologies to stay competitive and capitalise on the digital market's potential.

The outbreak of the COVID-19 crisis increased the stakes around digital access and engagement, reinforcing the importance of communications infrastructure and the use of digital technologies to enhance small and medium-sized enterprises' (SMEs) resilience (OECD, 2020[3]). Embracing digital technologies brings several benefits to SMEs, offsetting some size-related structural limitations and improving firm performance in terms of growth, innovation, and internationalisation, as well as competitiveness:

- **Digitalisation enables SMEs to expand their customer reach and access global markets through e-commerce platforms**, reducing transport costs and making services internationally tradeable (OECD, 2021[4]). This leads to increased customer bases, revenues, and productivity and lowers marginal costs.
- **Digital technologies allow SMEs access to strategic resources**, such as financing through peer-to-peer lending and borrowing platforms (OECD, 2021[4]). They also allow SMEs to broaden their recruitment channels and facilitate access to online training and digital government services.
- **Digital platforms help SMEs capitalise on network effects** by outsourcing business functions, enhancing collaboration, information sharing and communication within and between organisations (OECD, 2021[1]).
- **Digital technologies enhance decision making** by providing real-time data and predictive analytics (Devops, 2021[5]). Using digital tools, such as predictive modelling software and dashboards, allows for data-driven decision making, experimentation and further innovation.
- **Digital tools increase agility and resilience**, enabling businesses to gain a competitive advantage and better weather crises. As products continuously evolve and customer demands shift while reliable revenue streams diminish, businesses that have adopted digital technologies can swiftly adapt.

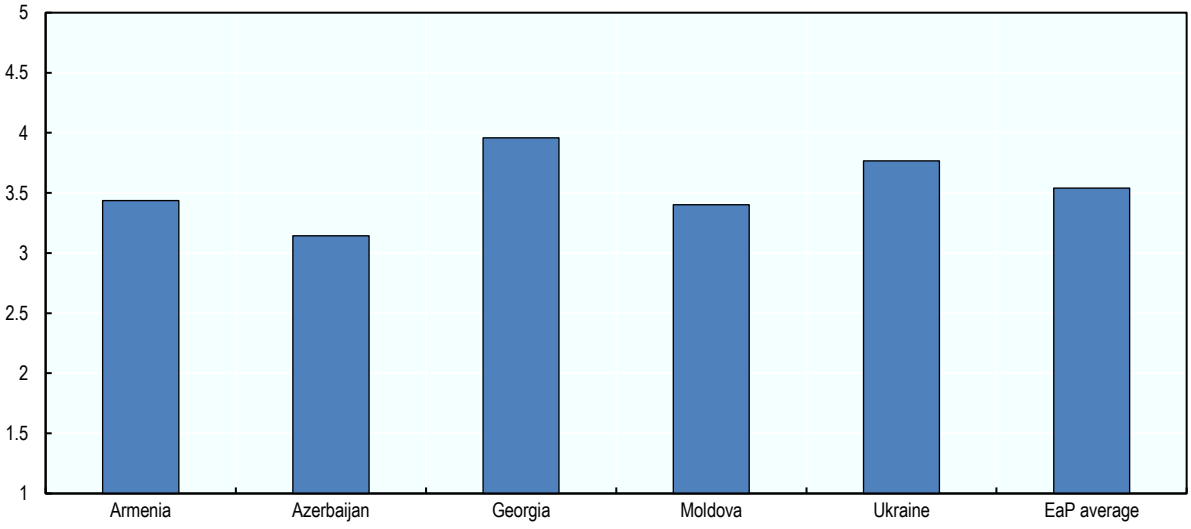
Despite this potential, SMEs in the Eastern Partner (EaP) region have yet to fully harness the benefits offered by digital solutions and, as in other regions, lag behind large firms in this regard. However, governments across the region have been working on addressing this issue and fostering further digitalisation. To support this impetus, the OECD has developed an encompassing analytical framework for supporting the digital transformation of SMEs, considering both technology adoption and digital culture (OECD, 2021[1]). The framework consists of a twofold approach, focusing on i) improving framework conditions for the digital economy and ii) implementing specific policy instruments to support SME digitalisation.

On the one hand, the framework conditions correspond to the prerequisites for a successful digital transformation – notably, broadband connectivity and physical infrastructure, as well as digital literacy across citizens. Indeed, ensuring an accessible, affordable and dependable Internet connection is vital to promoting the broader participation of individuals and businesses in the digital economy and preventing digital divides between urban and rural areas, as well as between SMEs and larger firms. As for digital literacy, enabling the acquisition of digital skills at all stages of life – through well-designed school curricula and lifelong learning opportunities for adult skills development – is necessary to equip both present and future employees with the skills required to embark on digital transformation, create tech-savvy consumers and develop a talent pool of IT specialists.

On the other hand, beyond these fundamental enablers, SMEs also need targeted policy measures to encourage them in their digitalisation journey, for example, through specific business support services, digital financial services, and help to tap into the potential of e-commerce.

Considering the increasing and strategic importance of the topic, this new round of the Small Business Act (SBA) assessment grants particular attention to digitalisation, reflecting the OECD's twofold approach in its analysis: a pillar on selected framework conditions for the digital transformation has been added, assessing national digital strategies, measures for broadband connectivity and digital skills, while new sub-dimensions have been incorporated to pre-existing pillars to provide for an in-depth study of SME digitalisation policies. The OECD calculated a weighted average of the scores from the pillar on selected framework conditions for the digital transformation and cross-cutting sub-dimensions in other parts of the SME Policy Index, resulting in overall composite scores for SME digitalisation policies (Figure 4.1, Table 4.1)

## Figure 4.1. Composite scores for SME digitalisation policies in EaP countries




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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## Table 4.1. Policy frameworks for SME digitalisation, scores by component

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Composite scores for SME digitalisation policies** | **3.44** | **3.14** | **3.96** | **3.40** | **3.77** | **3.54** |
| Selected framework conditions for the digital transformation | 3.92 | 2.96 | 4.02 | 3.22 | 3.93 | 3.61 |
| 3.4 Institutional framework for SME digitalisation | 3.50 | 4.05 | 4.54 | 4.20 | 4.40 | 4.14 |
| 4.1 E-government services | 4.00 | 4.25 | 4.29 | 4.34 | 4.66 | 4.31 |
| 5a.3 Support services for digital transformation of SMEs | 3.11 | 2.91 | 3.59 | 3.51 | 3.53 | 3.33 |
| 6.6 Digital financial services | 3.52 | 3.05 | 3.94 | 3.02 | 3.81 | 3.47 |
| 7.4 Digitalisation of standards and technical regulations | 1.50 | 2.13 | 3.63 | 2.50 | 2.50 | 2.45 |
| 10.4 Use of e-commerce | 2.25 | 3.44 | 4.00 | 3.31 | 2.89 | 3.18 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Assessment framework

The composite scores for the SME digitalisation policies presented above reflect the assessment of selected framework conditions for the digital transformation and cross-cutting, digitalisation-oriented sub-dimensions integrated into other pillars of the SME Policy Index.

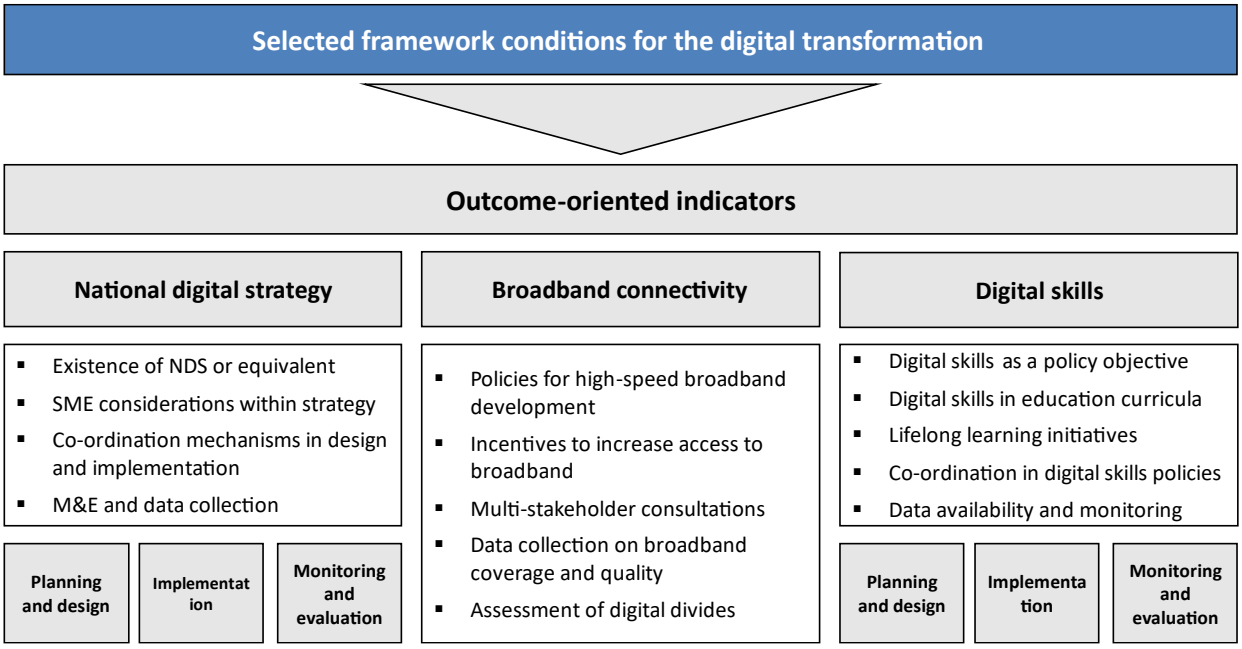
### *Selected framework conditions for the digital transformation*

This new pillar assesses the state of selected framework conditions for the digital transformation in EaP countries, looking at i) the overall policy framework (the national digital strategy or equivalent), ii) broadband connectivity and iii) digital skills.

As a result, the assessment framework is composed of the following elements:

- **National digital strategy** looks at the existence of a national digital strategy and/or other policy document designed to accelerate the digital transformation. It considers the measures planned, including for SMEs; budget, targets and monitoring practices; and the co-ordination mechanisms introduced among public and private bodies/actors for policy design and implementation.
- **Broadband connectivity** takes stock of efforts to increase access to high-speed Internet across individuals and firms, including dedicated policies; government investment in infrastructure; incentives for households, businesses, and broadband providers; and 5G provisions. Emphasis is also placed on data collection and an assessment of digital divides.
- The section on **digital skills** focuses on policies to help citizens of all ages become digitally literate. It assesses policy documents, the involvement and co-ordination of relevant stakeholders, and measures to both include digital competence in school curricula and introduce lifelong learning opportunities for digital skills development. It also pays particular attention to data collection on digital skills levels, monitoring and evaluation, skills anticipation exercises, and steps taken to respond to the European Union's (EU) digital competence framework (DigComp).
- The section on **outcome-oriented indicators** considers countries' ability to regularly collect statistical information about the following indicators: i) fixed broadband subscriptions per 100 inhabitants; ii) mobile broadband subscriptions per 100 inhabitants; iii) share of households with broadband connections; iv) share of businesses with broadband contracted speed of 30 Mbps or more; v) disparity in broadband uptake between urban and rural households; vi) share of individuals using the internet to interact with public authorities; vii) new tertiary graduates in science, technology, engineering and mathematics, as a percentage of new graduates; viii) ICT skills (basic, standard, advanced); and ix) students' (15-year -old) performance in reading, mathematics, and science.

### Figure 4.2. Assessment framework – selected framework conditions for the digital transformation




Note: NDS: National digital strategy. M&E: monitoring and evaluation.

### *Digitalisation-oriented sub-dimensions*

Beyond these selected framework conditions, the composite scores for SME digitalisation policies also include results from digitalisation-oriented sub-dimensions included in other parts of the SBA assessment, namely:

- The **Institutional framework for SME digitalisation** sub-dimension analyses whether and how support for SME digitalisation is embedded in SME policies. For more information, see the Pillar A chapter.
- The **E-government services** sub-dimension assesses governments' strategy for providing e-services, the range of services provided, the level of interoperability among the different data banks run by the public administration, and action taken to implement an open data approach. For more information, see the Pillar A chapter.
- The **Business support services for the digital transformation of SMEs** sub-dimension looks at government-led initiatives to support the digital transformation of SMEs – e.g. information support, training, financial instruments and advisory services to better understand company needs, procure digital technologies and develop tailored digital roadmaps. For more information, see the Pillar E chapter.
- The **Digital financial services** sub-dimension covers the existence of a regulatory and supervisory framework for a range of digital financial services. For more information, see the Pillar C chapter.
- The **Digitalisation of standards and technical regulations** sub-dimension evaluates support and training offered to SMEs on standards and technical regulations for their integration into the EU Digital Single Market; the digitalisation of processes within authorities responsible for technical regulation, national standards and accreditation bodies, metrology institutes and market surveillance authorities; and the introduction by accreditation bodies, conformity assessment bodies and surveillance authorities of remote audit and inspection activities. For more information, see the Pillar D chapter.

- The **Use of e-commerce** sub-dimension investigates efforts to encourage more widespread use of e-commerce as a sales channel by SMEs, considering both regulatory aspects and government policies to promote SMEs' access to digital platforms and the provision of support services to remove barriers that prevent SMEs from benefitting from growing trade digitalisation. For more information, see the Pillar D chapter.

The following sections outline the main findings and policy options for selected framework conditions for the digital transformation, followed by a summary of the assessment of the digitalisation-oriented sub-dimensions. A detailed analysis of the sub-dimensions can be found in the respective pillars.

## Selected framework conditions for the digital transformation

### *National digital strategy*

National digital strategies appear as a key tool for countries to accelerate the digital transformation of their economy and society. They usually appear as a comprehensive tool outlining the government's overall approach to the topic, entailing the main policy priorities and objectives in this regard, and facilitating coherence and stakeholder co-ordination (Gierten and Lesher, 2022[6]).

#### *Analysis*

All EaP countries have made digitalisation a policy priority. They have been developing policy frameworks to this end, although these differ in nature and scope: so far, Armenia is the only country in the region to have adopted a national digital strategy (NDS), the *Digitalisation Strategy of Armenia for 2021-2025*, which aims at ensuring a data-driven public administration, modernising the economy and increasing competitiveness through digital solutions, and fostering digital skills development. Azerbaijan, Georgia and Moldova have prepared multi-year strategies that are currently awaiting approval and should be adopted by the end of 2023. Policy objectives are currently scattered across different policy documents, whether they be overarching country strategies as in Azerbaijan and Georgia, or innovation strategy as in Moldova. Georgia also has digitalisation-related provisions in its ongoing broadband and SME strategies. In the case of Ukraine, the country's strategic vision for the digital transformation has been embedded in several government documents[1], including the *National Economic Strategy 2030*, and further plans to step up policy efforts for post-war recovery are reflected in the Draft Recovery Plan.

However, existing policy documents for the digital transformation pay only limited attention to the digitalisation of SMEs in non-IT sectors. Armenia's NDS includes provisions to accelerate SME digitalisation, notably by raising private sector awareness of digital tools, increasing businesses' use of new technologies, and further developing e-commerce and innovative solutions. Other EaP countries have planned a few measures in their strategies, but these remain scarcer and often limited to digital skills. However, implementation has sometimes happened outside policy strategies – Georgia and Moldova, for instance, have launched dedicated programmes to support SME digitalisation (for the first time in 2023 and 2020, respectively), although these are not part of ongoing policy documents[2].

In terms of policy governance, all EaP countries have been working to develop multi-stakeholder approaches. The design of strategic policy documents for digitalisation has benefitted from the involvement and contributions of a wide range of actors, most often through the establishment of dedicated working groups encompassing ministries, public agencies, international experts (consulting firms and/or international organisations) and sometimes businesses and business associations. These mechanisms, along with the clear mandates given to one stakeholder to lead the NDS, have also allowed for co-ordination among actors. Moving forward, countries should pursue a continued multi-stakeholder approach to policy implementation, which is not yet systematic across the region. While some countries, such as Armenia and Moldova, have taken steps in that direction with their digitalisation councils and public-private

working groups planned for specific topics in their respective ongoing and draft NDSs, policy makers across the region should ensure that all concerned parties are involved– including Ministries of Labour and employment agencies, actors that may be newer to digitalisation policies (such as tax offices), and the business community. These are essential for the comprehensiveness and successful implementation of the NDS (Gierten and Lesher, 2022[6]).

One of the main weaknesses for most EaP countries remains data collection on the digital transformation, which is essential for monitoring and evaluation. Apart from insights into broadband connectivity (further detailed in the following section national statistical offices collect only a limited number of indicators, and rarely on businesses' uptake and use of digital tools. Georgia and Ukraine appear as frontrunners in this regard, while Azerbaijan has recently achieved considerable progress, but more could be done to align with OECD and EU methodologies. As a result, current policy documents lack targets to assess progress, e.g. on digital skills development and SME digitalisation.

### *The way forward*

Moving forward, EaP countries could complement and strengthen their policy frameworks for the digital transformation by:

- **Consolidating policy approaches to digitalisation and ensuring co-ordination throughout strategy implementation**: Each EaP country should adopt a comprehensive NDS encompassing all relevant domains for the digital transformation, setting clear objectives associated with measurable targets, and a corresponding budget. The involvement and co-ordination of all concerned public and private stakeholders should be ensured throughout implementation to allow for successful execution and feedback. The OECD recently published a methodology for assessing NDSs and their governance across member countries, based on the OECD Going Digital Integrated Policy Framework, which can serve as a useful reference (Box 4.1).
- **Including provisions for SME digitalisation in overarching policy documents**: More attention should be paid to the digital transformation of small businesses in non-IT sectors. Policy makers should adopt a comprehensive approach to foster this transition, considering both technology adoption and digital culture.
- **Improving monitoring and evaluation by setting result-oriented key performance indicators and collecting internationally comparable data**: Countries should make further efforts to collect data on the digital transformation, including that of businesses, by size, in line with OECD/EU methodologies. Table 4.2 provides an overview of the key indicators underpinning the OECD Going Integrated Policy Digital Framework. The OECD database on ICT Access and Usage by Businesses, as well as the EU Digital Economy and Society Index (DESI), offer additional useful references for firms' digitalisation specifically.

### Box 4.1. OECD methodology for assessing national digital strategies and their governance

The OECD Going Digital Integrated Policy Framework assists governments in developing coherent and resilient policies to realise the potential of digital transformation and address its challenges. The Framework evaluates NDS comprehensiveness across 38 policy domains, organised into seven overarching dimensions that collectively enhance growth and well-being:

- **Access** to communications infrastructures, services, and data
- Effective **use** of digital technologies and data
- Data-driven and digital **innovation**
- Good **jobs** for all
- **Social** prosperity and inclusion
- **Trust** in digital environments
- **Market openness** in digital business.

Policy makers can gain valuable insights by assessing their NDS strengths and weaknesses and understanding the comprehensiveness of other countries' NDSs to help identify policies for enhancing their own strategy. Successful NDS development and implementation requires effective governance. While governance is often country-specific and shaped by domestic factors, several aspects help distinguish different types of approaches and identify respective strengths:

***Strategy responsibilities***

A comprehensive NDS involves various stakeholders, both within and outside the government, requiring effective co-ordination. Strategic responsibility should be assigned to a high-level body or a dedicated Ministry for Digital Affairs to ensure success.

***Co-ordination arrangements***

Effective NDS co-ordination involves two main arrangements: 1) co-ordination groups/committees involving government actors during strategy development and implementation; and 2) one-off consultations with multiple stakeholders, often online, to address specific co-ordination tasks, especially during strategy development.

***Funding implementation***

NDS implementation requires funding, either explicitly attached or obtained from decentralised sources. An attached budget aids co-ordination and oversight for greater success of the strategy. Decentralised funding may impact accountability and the effectiveness of the strategy. In countries with an explicitly attached budget, strategic co-ordination is often allocated to a high-level body or a ministry dedicated to digital affairs.

***Monitoring implementation***

To oversee the progress of an NDS, countries must monitor its implementation by setting measurable targets, collecting data and using relevant indicators. Monitoring is typically carried out by the body responsible for NDS development, especially in countries with a dedicated Ministry for Digital Affairs. Alternatively, a co-ordination group of key actors involved in implementation may also oversee monitoring. Some countries integrate specific policy measures with indicators to measure their implementation and effects.

Source: (Gierten and Lesher, 2022[6]).

## Table 4.2. Key indicators underpinning the OECD Going Digital's seven policy dimensions

| Policy dimension | Indicator | 2022 OECD values |
|---|---|---|
| Access | Fixed broadband subscriptions per 100 inhabitants | 34.9 |
| | M2M (machine-to-machine) SIM cards per 100 inhabitants | 36.1 |
| | Mobile broadband subscriptions per 100 inhabitants | 127.9 |
| | Share of households with broadband connections | 90.8% |
| | Share of businesses with broadband contracted speed of 30Mbps or more | 79.3% |
| | Share of the population covered by at least a 4G mobile network | 98.2% |
| | Disparity in broadband uptake between urban and rural households | 3.83pp |
| Use | Internet users as a share of individuals | 91.4% |
| | Share of individuals using the Internet to interact with public authorities | 60% |
| | Share of Internet users who have purchased online | 72% |
| | Share of small businesses making e-commerce sales | 26.1% |
| | Share of businesses with a web presence | 78.1% |
| | Share of businesses purchasing cloud services | 45% |
| | Average monthly mobile data usage per mobile broadband subscriptions | 10.4Gb |
| | Share of adults proficient at problem solving in technology-rich environments | 30.6% |
| Innovation | ICT investment as a share of GDP | 2.37% |
| | Business R&D expenditure in information industries as a share of GDP | 0.433% |
| | Venture capital investment in the ICT sector as a share of GDP | 0.09406% |
| | Start-up firms (up to 2 years old) in information industries as a share of all businesses | 24.4% |
| | Top 10% most-cited documents in computer science, as a share of the top 10% ranked documents in all fields | 6.52% |
| | Patents in ICT technologies, as a share of total IP5 patent families | 31% |
| Jobs | Share of ICT task-intensive jobs | 13.9% |
| | Digital-intensive sectors' share in total employment | 49.4% |
| | Workers receiving employment-based training as a share of total employment | 59.2% |
| | Share of individuals who use digital equipment at work that telework from home once a week or more | 26.4% |
| | New tertiary graduates in science, technology, engineering, and mathematics as a share of new graduates | 23.4% |
| | Public spending on active labour market policies as a share of GDP | 0.832% |
| Society | Share of individuals aged 55-74 years using the Internet | 78.8% |
| | Share of individuals who live in households with income in the lowest quintile who use the Internet | 83.6% |
| | Women as a share of all 16–24-year-olds who can program | 29.7% |
| | Disparity in Internet use between men and women | 0.43pp |
| | Top-performing 15–16-year-old students in science, mathematics and reading | 15.3% |
| | OECD Digital Government Index | 0.51 |
| | E-waste generated per capita | 17.286kg |
| Trust | Share of Internet users experiencing abuse of personal information or privacy violations | 3.99% |
| | Share of Internet users not buying online due to payment security concerns | 22.5% |
| | Share of Internet users not buying online due to concerns about returning products | 5.49% |
| | Share of enterprises in which own employees carry out ICT security related activities | 42.8% |
| | Health data sharing intensity | 65.2% |
| Market openness | Share of businesses making e-commerce sales that sell across borders | 40.1% |
| | Digitally deliverable services as a share of commercial services trade | 37.5% |
| | ICT goods and services as a share of international trade | 12.2% |
| | Digital-intensive services value added embodied in manufacturing exports as a share of manufacturing export value | 23.6% |
| | OECD Digital Services Trade Restrictiveness Index | 0.14 |
| | OECD Foreign Direct Investment Regulatory Restrictiveness Index | 0.06 |

Notes: Mbps: megabits per second; GDP: gross domestic product; R&D: research and development; pp: percentage point; Gb: gigabyte; kg: kilogramme; IP5: patents filed in at least two offices worldwide, including one of the five largest IP offices. OECD values refer to the average for OECD countries for which data is available. Data is provided for 2022 or the most recent year available.
Source: (OECD, 2022[7]).

### *Broadband connectivity*

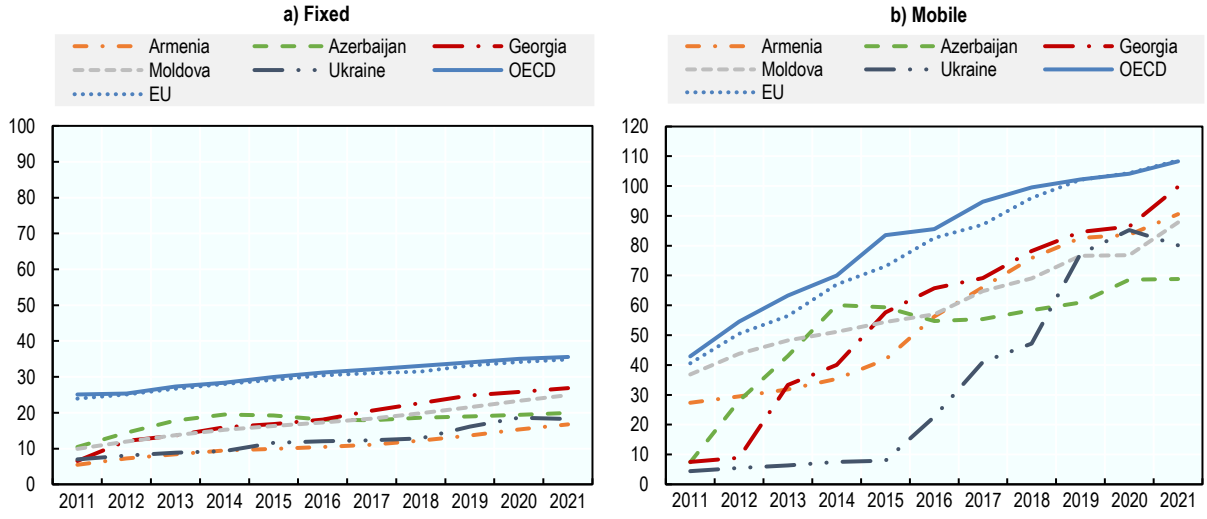
Guaranteeing efficient, affordable and reliable access to the Internet is a pre-requisite for economies and societies to tap into the potential of the digital transformation. Some OECD countries recognise it as a basic right, while "providing universal and affordable access to the Internet" is listed among the United Nations Sustainable Development Goals (SDGs).

#### *Analysis*

Broadband uptake has been steadily increasing in EaP countries over recent years, although significant disparities remain between countries. Georgia appears as the most connected EaP state, while Ukraine registers the fastest progress, with the number of fixed and active mobile subscriptions increasing by 52% and 254%, respectively, between 2016 and 2021. However, despite these advances, connectivity levels in the EaP region still lag OECD and EU values (Figure 4.3).

**Figure 4.3. Broadband uptake in Eastern Partner, OECD and European Union countries, 2011-21**

Fixed and active mobile subscriptions per 100 inhabitants



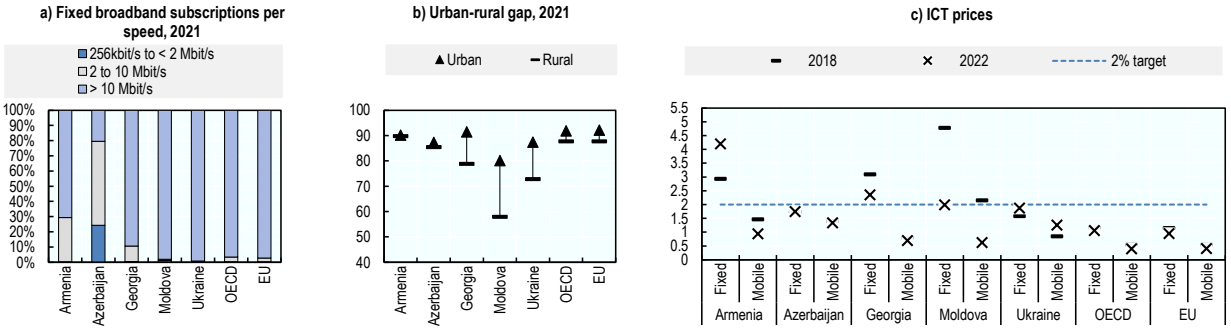

Note: OECD and EU correspond to median values.
Source: Based on (ITU, 2022[8]).

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Beyond uptake, access to quality broadband at affordable prices is essential for individuals and firms to reap the benefits of digitalisation. Recent data highlight persistent regional disparities across the EaP region: while almost all fixed broadband subscriptions in Moldova and Ukraine benefit from a good connection speed – i.e. above 10 Mbps, similar to OECD and EU levels – Internet speed still poses a challenge in Azerbaijan (Figure 4.4). Moreover, all countries have been working to foster equal access to the Internet across their respective territories, but digital divides remain, especially in Georgia, Moldova, and Ukraine. Overall, broadband uptake is challenged by prices: although ICT prices appear among the cheapest worldwide in absolute terms, tariffs expressed as a percentage of gross national income per capita show that Internet remains less affordable in the EaP region than in OECD and EU countries – especially for fixed broadband. Armenia and Georgia were still above the International Telecommunication Union's target of 2% of monthly GNI per capita in 2022, while Moldova, after considerable improvements in recent years, reached 2%. This can hamper firms' uptake, as businesses require strong, fast and reliable

connections to conduct online operations – a demand better matched by fixed broadband, which often offers a higher speed, e.g. for running software.

## Figure 4.4. Broadband quality, coverage, and affordability in Eastern Partner, OECD and EU countries




Notes: Mbps: megabits per second; EU: European Union. OECD and EU values correspond to median values for member states for which 2021 data is available. EU-8 = Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic and Slovenia.
Source: OECD calculations based on (ITU, 2022[8]).

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With regard to businesses' broadband uptake and speed, data remain scarce across EaP countries. Only Georgia and Ukraine collect such size-disaggregated indicators, which show that firms' connectivity lags behind that of OECD and EU countries. The gap between SMEs and large firms is also more significant: in Ukraine, for instance, 84.5% of small firms have access to the Internet (10 percentage points [p.p.] Internet compared to larger firms), vs. 96% in the OECD (-3 p.p. compared to larger firms). Moreover, most small Georgian companies do not have access to high-speed Internet (Geostat, 2022[9]).

Policymakers across the EaP region have taken measures to address these remaining challenges and tackle digital divides. Georgia has made the development of high-speed Internet a priority, fostering it through a dedicated broadband strategy aiming at increasing competitive pressure, attracting investments, and building digital skills and demand. Armenia and Ukraine have been developing their own broadband plans, though they are yet to be finalised and adopted. Current national broadband policies in EaP countries most often include provisions to develop fibre and/or 5G and to further invest in infrastructure development.

However, broadband policies could benefit from more regular consultations with relevant stakeholders in some countries. Indeed, continued multi-stakeholder dialogue involving consumers, network operators, local governments and regulatory authorities can help to ensure that all parties' opinions are adequately taken into account (OECD, 2021[10]).

### *The way forward*

Moving forward, EaP countries could further enhance broadband connectivity across their respective territories and address remaining digital divides across individuals and firms, notably the affordability of fixed broadband. This could be promoted by:

- **Fostering competition**, for example by promoting co-investment, infrastructure sharing, and adequate legal and regulatory frameworks. The legal and regulatory frameworks should be reviewed regularly to ensure their continued adequacy. To this end, EaP countries should conduct

regular multi-stakeholder consultations on Internet connectivity, to provide for evidence-based policy making.

- **Increasing demand for quality broadband by fostering digital literacy among citizens and firms**. Countries could, *inter alia*, strengthen consumer rights and choice by eliminating information asymmetries and providing open and reliable data on subscriptions, coverage and quality of service, thereby helping consumers take informed decisions while incentivising Internet providers to enhance network quality.

Overall, EaP countries can refer to the OECD's *Recommendation of the Council on Broadband Connectivity* for further guidance (OECD, 2021[10]).

### *Digital skills*

Digital skills are at the core of the digital transformation. The swift development of digital technologies has been triggering changes in labour markets, with some skills becoming redundant due to automation while digital skills are increasingly in demand. Therefore, providing relevant education, along with lifelong learning opportunities is essential to help individuals meet evolving labour market requirements. Equipping employees with digital competences is also crucial for firms, as the availability of a digitally literate workforce and investment in skills training are associated with higher adoption levels of digital technologies.

The present analysis considers the three main categories of digital skills as outlined in previous OECD work[3] – 1) ICT generic skills (i.e. the capacity for any working-age individual to make use of new technologies), 2) ICT advanced skills (i.e. the competences acquired by IT specialists), and 3) ICT complementary skills ("softer" skills, e.g. problem-solving, information processing, and communication).

#### *Analysis*

Digital skills are embedded in policy documents related to digitalisation across the EaP region. All countries have made good progress in including digital competence in education systems. It is now part of national education curricula, at least for one level of education. Armenia and Moldova have included it as a key competence for all education levels, with a core course on digital education/informatics and additional, optional modules on specific topics. Georgia has focused its digital literacy efforts in formal education on vocational education and training (VET) so far. Moreover, the COVID-19 pandemic has accelerated the development of online education for pupils and students, as containment measures forced educational institutions to move classes to dedicated web platforms. These measures have been accompanied in most countries by some teacher training.

EaP countries have also been working towards providing their citizens an increasing number of lifelong learning opportunities on digital skills development. Several projects have been carried out to this end, such as the Digital Academy and IT Hubs in Azerbaijan, or the wide range of online courses offered by Georgia's Innovation and Technology Agency. As a common feature appearing across the region, the active involvement of the private sector has been enhancing these training opportunities. Tekwill, for instance, is the flagship private initiative in Moldova in this regard (see Box 13.2 in the Moldova country chapter), while Armenia benefits from a growing number of educational centres and programmes, such as the TUMO Centre for Creative Technologies and the Armath educational programme (Box 4.2). However, support for digital skills development among small firms specifically remains limited across the region.

## Box 4.2. Selected digital skills initiatives in Armenia

### TUMO Centre for Creative Technologies

Armenia's TUMO Centre for Creative Technologies is a non-profit organisation providing free education in diverse creative and technological disciplines to youth aged 12-18. The TUMO programme employs a combination of guided self-learning and project-based learning, fostering real-world experiences for students and offering companies access to a pool of emerging talent. Sub-programmes include:

- **TUMO Labs** focuses on delivering advanced and in-depth training in technology, creative industries, and entrepreneurship. It nurtures young talent, offering resources, mentorship and real-world exposure in collaboration with industry professionals and companies.
- The **EU TUMO Convergence Centre** caters to university students and emerging professionals, fostering a collaborative environment and bringing together students, partners, local businesses, and universities to maximise opportunities for all stakeholders in the region.
- **42 Yerevan** is a tuition-free programming school for students over 18 that offers guided self-learning programmes in technology, applied science and engineering. It boasts a 95% job placement success rate for graduates.

In addition to offering free access to quality education, TUMO implements several good practices in its education approach, encompassing:

- project-based learning and interdisciplinary approach, with TUMO's curriculum revolving around hands-on projects; enriching students' skills across diverse disciplines; and encouraging the exploration and integration of programming, design, animation, robotics and more
- digital and creative skills, with the programme nurturing digital literacy and creativity to meet the demands of the digital era and creative industries
- state-of-the-art facilities with cutting-edge technology for innovative learning environments
- professional mentorship, with industry experts guiding students' learning and development
- collaboration with industry, offering real-world projects and career pathways
- social and cultural activities as TUMO facilitates community-building and collaboration
- lifelong learning, encouraging students to remain curious beyond their time at the centre.

### Armath educational programme

Launched in 2014, Armath aims to promote science, technology, engineering and mathematics (STEM) education among schoolchildren, thereby cultivating a new generation of innovators in Armenia. The programme has yielded a range of significant outcomes by:

- stimulating technological education across the country
- promoting regional development and improving conditions in borderline communities
- fostering an entrepreneurial culture and boosting economic activity in high-tech sectors

strengthening the bond between the education system, the labour market and the universities. The Armath Engineering Laboratories programme had demonstrated promising outcomes by 2022, with 45% of Armath students admitted to regional and 3% to international universities, 11% finding employment in the IT sector and 1% founding start-ups.

Source: (TUMO Center for Creative Technologies, 2023[11]), (TUMO Labs, 2023[12]), (Armath, 2023[13]).

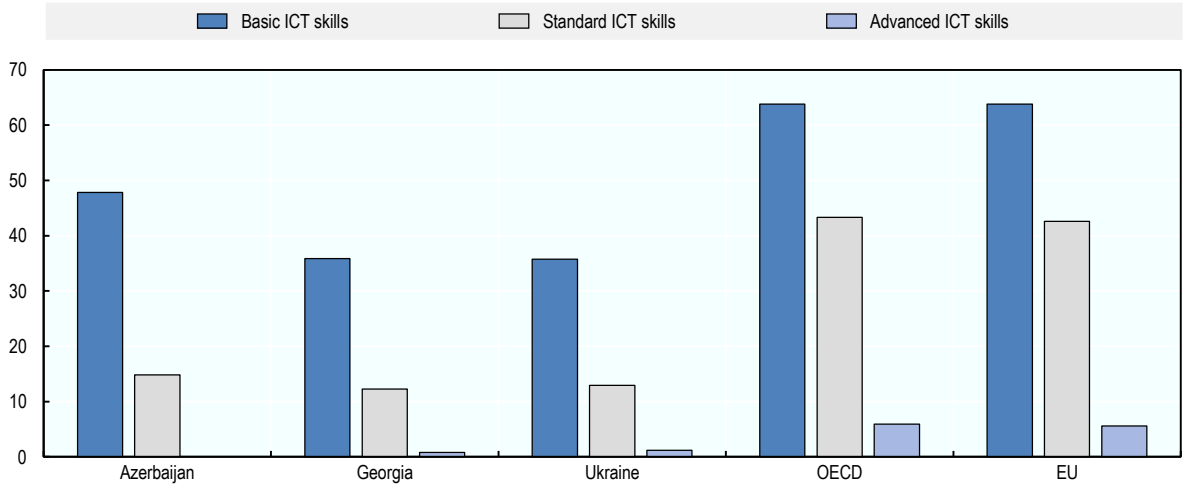
Overall, Ukraine comes out as the EaP leader in the field, having developed the most comprehensive policy approach to digital skills development. It has implemented a wide range of initiatives and tools to this end, most often in line with EU practices. It notably appears as the only country in the region to have implemented a self-assessment tool for individuals to evaluate their digital skills, as well as a digital competence framework to serve as a reference, following the example of EU's DigComp 2.1. Based on this framework, the online platform Diia.Digital Education offers a wide range of free digital literacy courses for citizens, and the National Online School for Entrepreneurs provides additional resources for small businesses.

Nevertheless, digital skills levels across the region remain below OECD and EU levels (Figure 4.5). Overall, data on digital literacy appears to be quite scarce – Armenia and Moldova do not collect such insights, and data on digital skills among firms are still very limited. This poses an issue for monitoring and evaluation purposes, and evidence-based policy making in general. Beyond data collection, skills assessment and anticipation exercises remain nascent in EaP countries: apart from Georgia, countries do not yet have a systemic approach. Labour market forecasts, when implemented, do not entail digital skills aspects – e.g. in Moldova. By and large, digital skills assessment and anticipation practices, such as surveys and/or sectoral studies, are most often conducted on an ad hoc basis, by donors/development partners.

Finally, while several ministries and governmental agencies are involved in elaborating digital skills policies, the policies would benefit from greater involvement of certain relevant yet often overlooked stakeholders: Ministries of Labour, national employment agencies, but also teachers and private sector representatives.

## Figure 4.5. Individuals with ICT skills in Eastern Partner, OECD and European Union countries

Percentage of individuals with skills, 2021




Note: Data not available for Armenia and Azerbaijan. Data on advanced skills for Georgia refer to 2020, as 2021 data are not available. Data on advanced skills for Azerbaijan not available. OECD and EU values refer to the median values of countries for which 2021 data is available. Basic skills correspond to copying or moving a file or folder, using copy and paste tools, sending e-mails with attached files, and transferring files between a computer and other devices; standard skills to using basic arithmetic formula in a spreadsheet; connecting and installing new devices; creating electronic presentations with presentation software; and finding, downloading, installing and configuring software; and advanced skills to writing a computer program using a specialised programming language.
Source: Based on (ITU, 2022[8]).

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*The way forward*

Moving forward, EaP countries could step up their efforts towards building digitally literate societies by:

- **Strengthening multi-stakeholder approaches to digital skills development** by ensuring the participation of all relevant stakeholders in the policy making and implementation processes. Implementing national digital skills and jobs coalitions could be helpful in this regard.
- **Implementing digital skills as a key competence at all education levels** to ensure all citizens acquire ICT generic skills as part of their education. This should be accompanied by an assessment of learning outcomes.
- **Adopting a framework for digital competences to serve as a common reference**, following the example of DigComp 2.1 (Box 4.3). Such a framework will help the assessment and certification of the digital competences acquired while building a common understanding of digital skills across countries.
- **Developing digital skills assessment and anticipation tools** – e.g., improving data collection on levels of digital skills among the population and in firms; introducing self-assessment tools for individuals to evaluate their competences and identify their training needs; and conducting anticipation exercises to inform future policies and training – in line with EU methodology to ensure comparability.
- **Stepping up support for digital skills development among firms, especially small ones.**

### Box 4.3. The Digital Competence Framework for Citizens (DigComp)

In response to the rapid technology advancements and the ever-growing significance of digital skills, the European Commission has introduced DigComp – a framework designed to shape and assess individuals' digital competences. It fosters digital literacy and empowers citizens to engage proficiently and responsibly in various contexts, including education, workforce training and policy development. DigComp is a comprehensive roadmap for assessing and developing digital competencies in individuals across age groups and professions. It surpasses technical expertise, embracing crucial abilities and attitudes for the effective use of digital tools in the complexities of the digital era.

The DigComp framework consists of 5 areas of digital competence, with 21 specific competences.

1. ***Information and data literacy***

This area equips individuals to find, evaluate and manage digital information responsibly. Key aspects include information retrieval, evaluation, data management, privacy and copyright. It enables informed decision making and active digital participation while safeguarding privacy and digital identity.

2. ***Communication and collaboration***

This competence area focuses on developing individuals' proficiency in using digital tools and platforms to effectively communicate, share information and collaborate with others. It emphasises clear and meaningful digital interactions, enabling collaborative and productive exchanges across various contexts and platforms.

3. ***Digital content creation***

The DigComp's digital content creation is designed to empower individuals with the skills to proficiently produce, edit and share digital content across various formats, including text, images, audio, and video. It plays a pivotal role in enabling the effective expression of ideas and fostering valuable contributions to the digital landscape with professionalism and creativity.

4. ***Safety***

The safety competence area encompasses the acquisition of essential knowledge and skills that enable individuals to ensure their security and privacy in the digital environment. This entails a comprehensive understanding of digital security measures, proficiently safeguarding personal data and adopting responsible online practices to effectively mitigate potential risks and threats.

5. ***Problem solving***

Problem solving encompasses the acquisition of adept skills in analysing and resolving challenges proficiently via the use of digital tools and technologies. This proficiency enables individuals to identify issues, devise innovative solutions and take informed decisions in the digital landscape.

DigComp facilitates the development of essential digital skills, enhancing individuals' employability in a technologically driven job market. It promotes digital inclusion and bridging the digital divide and fosters responsible digital citizenship. The framework aids policy makers in designing effective digital literacy initiatives and policies, fostering a competent and productive society.

Source: (European Commission, 2023[14]).

## Digitalisation-oriented sub-dimensions

With regard to the digitalisation-oriented sub-dimensions, EaP countries have been advancing at different paces. They register strong performance in terms of e-government services, which have been steadily expanding in recent years and the institutional framework for SME digitalisation has been strengthened. Despite some welcome efforts, more could be done to develop targeted business support services for SME digitalisation, digital financial services, and e-commerce. The digitalisation of standards and technical regulations appears as the weakest area of the assessment.

Table 4.3 summarises the main findings and recommendations at the regional level for each of the sub-dimensions included in the composite scores for SME digitalisation policies. The detailed analysis for each of them, as well as country-level details, can be found in the relevant chapters.

### Table 4.3. Summary of key findings – digitalisation-oriented sub-dimensions

| Sub-dimension | EaP average | Main achievements | Shortcomings | Policy recommendations |
|---|---|---|---|---|
| 3.4 Institutional framework for SME digitalisation | 4.14 | SME digitalisation mentioned in ARM, AZE and GEO strategic documents for SMEs<br>Development of dedicated actors, e.g. UKR's Ministry of Digital Transformation and the effective Diia platform, while AZE established a dedicated agency under the Ministry of Digitalization and Transport. | The process is still in an early phase and the resources EaP countries allocate to SME digitalisation are relatively limited. | - Increase the human and financial resources allocated to programs for supporting the digital transformation of SMEs and make sure that the SME Development Agencies have the necessary competencies to manage those programmes |
| 4.1 E-government services | 4.31 | EaP countries have significantly expanded e-government services, simplified accessibility and improved e-governance.<br>All countries have approved multi-year strategic documents to guide further e-government service expansion. | Progress has been limited in monitoring and evaluation due to scarce data on e-government service use by SMEs based on enterprise typology and location. | - Systematically collect data on the use of e-government services by different categories of SME (by size, type of ownership and location) to identify the type of enterprises that encounter more difficulties in accessing and using e-government services and map e-government service utilisation by SMEs.<br><br>- Improving data availability could lead to more targeted information campaigns and SME training, enhancing e-government utilization rates. |
| 5a.3 Business support services for the digital transformation of SMEs | 3.33 | Prioritisation of trainings on digitalisation-related topics varies among EaP countries; Georgia and Moldova are pioneers in developing SME digitalisation programmes, offering individualised assessments, company-specific digitalisation roadmaps, and financial support for digital technologies and advisory services. | Trainings do not fully cater to individual SME needs, necessitating specialised consultant services for tailored analysis and recommendations. | - Include dedicated measures for business development services (BDS) delivery in strategic documents.<br>- Ensure regional office sustainability.<br>- Embed single information portals with BDS ecosystem actors on SME agencies' websites.<br>- Develop dedicated SME support programs with focus on digital skills, roadmaps & financial aid for tech adoption.<br>- Improve evaluation of support programs' impact on SME performance.<br>- Expand collection of statistical indicators on tech adoption among firms. |
| 6.6 Digital financial services | 3.47 | All financial authorities have a department with a dedicated mandate to cover digital financial services. | Regulatory frameworks still at a nascent stage.<br><br>Lack of specific | - Develop strategic directions for digital financial service regulation and supervision and adopt a multi-disciplinary approach. First steps would be to adopt |

| Sub-dimension | EaP average | Main achievements | Shortcomings | Policy recommendations |
|---|---|---|---|---|
| | | The topic is starting to be addressed in policy documents (dedicated digital finance strategy in Ukraine, part of Georgia's central bank's strategy, digital payment strategy in Azerbaijan).<br>All countries have regulation in place around data protection and sharing as well as an operational resilience framework for financial service providers. | provisions for big tech solutions.<br><br>No systematic implementation of a multi-disciplinary approach to digital finance supervision.<br><br>Only Georgia has started working towards developing regulatory sandboxes. | a strategy document and equip regulators with the necessary human capital and tools to address looming challenges. Part of this process is a new, more open, approach to regulation in which both public and private stakeholders are regularly consulted. |
| 7.4 Digitalisation of standards and technical regulations | 2.45 | Most countries offer support and training to SMEs on standards and technical regulations and have a strategy for digitalising processes within the authorities responsible for technical regulation.<br>Remote participation in standardisation, audit and inspection is possible, except in Armenia and Azerbaijan. | Performance in this sub-dimension is overall relatively weak.<br>Designated staff or special working groups for the digitalisation of processes and activities within the area of technical regulation are missing, except in GEO.<br>No country provides remote audit and inspection for first-time accreditation. The digitalisation of market surveillance is still underdeveloped in the region except in Georgia. | - Improve market surveillance and differentiate it from inspection.<br>- Seek international recognition for the quality infrastructure.<br>- Develop SME-specific standards for education strategies.<br>- Implement financial measures to support SME participation in standardisation.<br>- Enhance digital maturity in technical regulation and conformity assessment.<br>- Establish export platforms for SMEs.<br>- Improve the regular evaluation of the technical regulation system and quality infrastructure.<br>- Continue good practices from Twinning projects even after their completion. |
| 10.4 Use of e-commerce | 3.18 | All EaP countries improved e-commerce policies, with basic regulatory frameworks for e-commerce being put in place, including provisions on hybrid retail, e-signatures, and electronic payments. Azerbaijan, Moldova and Ukraine adopted a regulatory framework on the commercial practices of paid advertisement. | EaP countries still do not align with EU frameworks in cross-border e-commerce. Issues remain in the e-commerce ecosystem, legal framework and standardisation aspects.<br>Need for further strengthening of legislative frameworks related to platforms, parcel delivery and consumer protection.<br>All countries except Georgia lack a monitoring mechanism and e-commerce Trustmark certification schemes. | – Improve monitoring and evaluation for export promotion agencies.<br>– Support SME integration into global value chains through assessment, linkages with multinational corporations and foreign direct investment incentives.<br>– Enhance the e-commerce regulatory framework and introduce Trustmark certification.<br>– Simplify and automate trade procedures, improve broader agency co-operation, and harmonise trade-related documents. |

Note: For more information, please see Pillar A for 3.4 Institutional framework for SME digitalisation and 4.1 Digital government for SMEs; Pillar C for 6.6 Digital financial services; Pillar D for 7.4 Digitalisation of Standards and Technical Regulations and 10.4 Use of E-commerce; and Pillar E for 5a.3 Business Support Services for the Digital Transformation of SMEs.

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## Notes

[1] These documents are listed and detailed in the Ukraine country profile.

[2] These programmes are further detailed and analysed under Pillar E, business development services dimension.

[3] See, for instance, (Grundke et al., 2018[15]).

# 5 Pillar A – Responsive Government

A robust SME policy hinges upon a well-structured framework integrating policy, institutions, and regulations, supported by streamlined administrative procedures and effective insolvency systems. This chapter examines the responsiveness of EaP governments to SME requirements across three key dimensions. Firstly, it evaluates the state of the institutional and regulatory framework governing SME policies, encompassing progress in the institutional setting, legislative simplification and RIA, public-private consultations, and the regulatory framework for SME digitalisation. Subsequently, the chapter analyses SMEs' operational environment, exploring aspects such as e-government services, business licensing, company registration, and tax compliance procedures for SMEs. Lastly, the chapter delves into bankruptcy and second chance provisions with a focus on preventive measures, survival and bankruptcy procedures, and second chance promotion. For each of the three dimensions, this chapter offers policy recommendations for the EaP region.

## Introduction

Entrepreneurs in both developed and emerging economies must navigate a complex structure of government regulations, standards and procedures. However, while regulations governing business operations are essential, their implementation can sometimes be subject to difficult and costly mandatory requirements, thereby hindering entrepreneurship and discouraging entrepreneurial activity (OECD, 2020[1]). In addition, navigating the legal environment and complying with regulations can be cumbersome for SMEs, as the associated fixed costs disproportionally affect them as a result of limited operational capacity and other size-related constraints (OECD, 2022[2]; European Commission, 2008[3]). As a result, SMEs often perceive government authorities as a source of bureaucracy and complex, heavy-handed regulation.

Establishing clear and transparent institutional and regulatory settings is therefore critical to guide entrepreneurial activity and prevent lack of transparency, unpredictability of regulation, and corruption from undermining the business environment and creating obstacles to entrepreneurship. Therefore, an effective and efficient institutional and regulatory framework is an essential prerequisite for promoting entrepreneurial risk-taking, encouraging investment and innovation, reducing informality and corruption, and ensuring fair competition among businesses of all sizes (OECD, 2017[4]).

An effective and transparent regulatory environment is key to fostering entrepreneurship and supporting SME development at all stages of the business cycle, including entry, investment and expansion, transfer, and exit. Crafting an effective SME policy that comprehensively addresses these aspects is a complex task due to the highly diversified nature of the SME population and the intersection of SME policy with multiple domains of policy making. To navigate this complexity successfully, governments must establish a clear and strategic vision for SME policy, while building a broad consensus amongst all stakeholders, including the business community and SME associations, NGOs, experts, and relevant partner organisations.

The “Responsive Government” pillar investigates recent reforms across EaP countries through an assessment of three policy dimensions: 1) the institutional and regulatory framework for SME policy, 2) the operational environment for SMEs, and 3) bankruptcy and second chance. Table 5.1 presents the progress achieved by EaP countries in these areas since 2020.

### Table 5.1. Pillar A: Country scores by dimension and sub-dimension (2024)

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2024 (CM)* |
|---|---|---|---|---|---|---|---|---|
| **Institutional and regulatory framework for SME policy** | **3.24** | **3.69** | **4.37** | **3.93** | **3.68** | **3.78** | ***3.72*** | ***3.61*** |
| Institutional setting | 3.02 | 4.14 | 4.62 | 3.83 | 3.70 | 3.86 | *3.90* | *4.06* |
| Legislative simplification and RIA | 3.03 | 2.90 | 3.50 | 3.35 | 3.27 | 3.21 | *3.16* | *3.13* |
| Public-private consultations | 4.16 | 3.40 | 4.65 | 4.27 | 4.26 | 4.15 | *4.03* | *3.49* |
| Institutional framework for SME digitalisation | 3.50 | 4.05 | 4.54 | 4.20 | 4.40 | 4.14 | - | - |
| Outcome-oriented indicators | 3.00 | 4.00 | 5.00 | 5.00 | 3.00 | 4.00 | - | - |
| **Operational environment** | **3.99** | **4.25** | **4.51** | **4.34** | **4.11** | **4.24** | ***4.37*** | ***3.77*** |
| E-government services | 4.00 | 4.25 | 4.29 | 4.34 | 4.66 | 4.31 | *4.49* | *3.76* |
| Business licenses | 3.66 | 3.96 | 5.00 | 4.69 | 4.40 | 4.34 | *4.33* | *3.99* |
| Company registration | 4.88 | 4.52 | 5.00 | 4.74 | 4.52 | 4.73 | *4.80* | *3.94* |
| Tax compliance procedures | 2.73 | 3.70 | 4.26 | 3.78 | 2.73 | 3.44 | *3.50* | *3.44* |
| Outcome-oriented indicators | 4.56 | 5.00 | 4.11 | 4.11 | 3.67 | 4.29 | - | - |
| **Bankruptcy and second chance** | **1.97** | **1.91** | **3.36** | **2.00** | **2.52** | **2.35** | ***3.10*** | ***2.87*** |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2024 (CM)* |
|---|---|---|---|---|---|---|---|---|
| Preventive measures | 1.34 | 1.69 | 3.24 | 1.46 | 1.75 | 1.90 | *3.02* | *2.28* |
| Survival and bankruptcy procedures | 2.74 | 2.15 | 4.13 | 2.72 | 3.39 | 3.03 | *4.04* | *3.74* |
| Promoting second chance | 1.00 | 1.33 | 2.33 | 1.00 | 1.83 | 1.50 | *1.50* | *2.00* |
| Outcome-oriented indicators | 2.71 | 2.71 | 2.71 | 2.71 | 2.71 | 2.71 | - | - |

Note: CM = comparable methodology; RIA = regulatory impact assessment. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Institutional and regulatory framework for SME policy

This dimension measures progress in establishing a well-functioning institutional and regulatory framework for SME policy making based on the "Think Small First"[1] principle, the application of regulatory impact analysis (RIA) for business-related legislation, and the organisation of effective public-private consultations.

The application of the "Think Small First" principle, as presented in the EU Small Business Act, encourages policy makers to give due consideration to the impact that policy change will have on SMEs. To be able to take SME needs into consideration at an early stage of policy development, governments would benefit from devising comprehensive SME strategies, based on a clear and consistent SME definition and data collection goals, as well as by establishing a functional operational agency for policy implementation. Given the horizontal nature of SME policy, a related SME strategy would need to be co-ordinated on a regular basis amongst all line ministries, government agencies and other institutions tasked with SME policy making and implementation. Dedicated action plans are required to set clear targets, define measurable indicators, and allocate responsibilities and resources for policy delivery. All SME-related policies should be linked to broader socio-economic or development objectives and should reflect the main business constraints identified in a given country and local context.

*Ex ante* and *ex post* regulatory impact analysis (RIA) has great potential to ensure the promotion of better laws with less uncertainty. Evaluating the costs, benefits and social impact of regulation for SMEs (the so-called "SME test"[2]) enables policy makers to adapt regulations to smaller firms' needs. In addition, implementing comprehensive public-private consultations while giving specific consideration to SME needs is a key requirement of the "Think Small First" principle.

### *Assessment framework*

This dimension includes elements such as the definition of what an SME is; the institutions in charge of elaborating, implementing, monitoring and evaluating SME policy at the national level; and the mechanisms for policy dialogue and co-ordination.

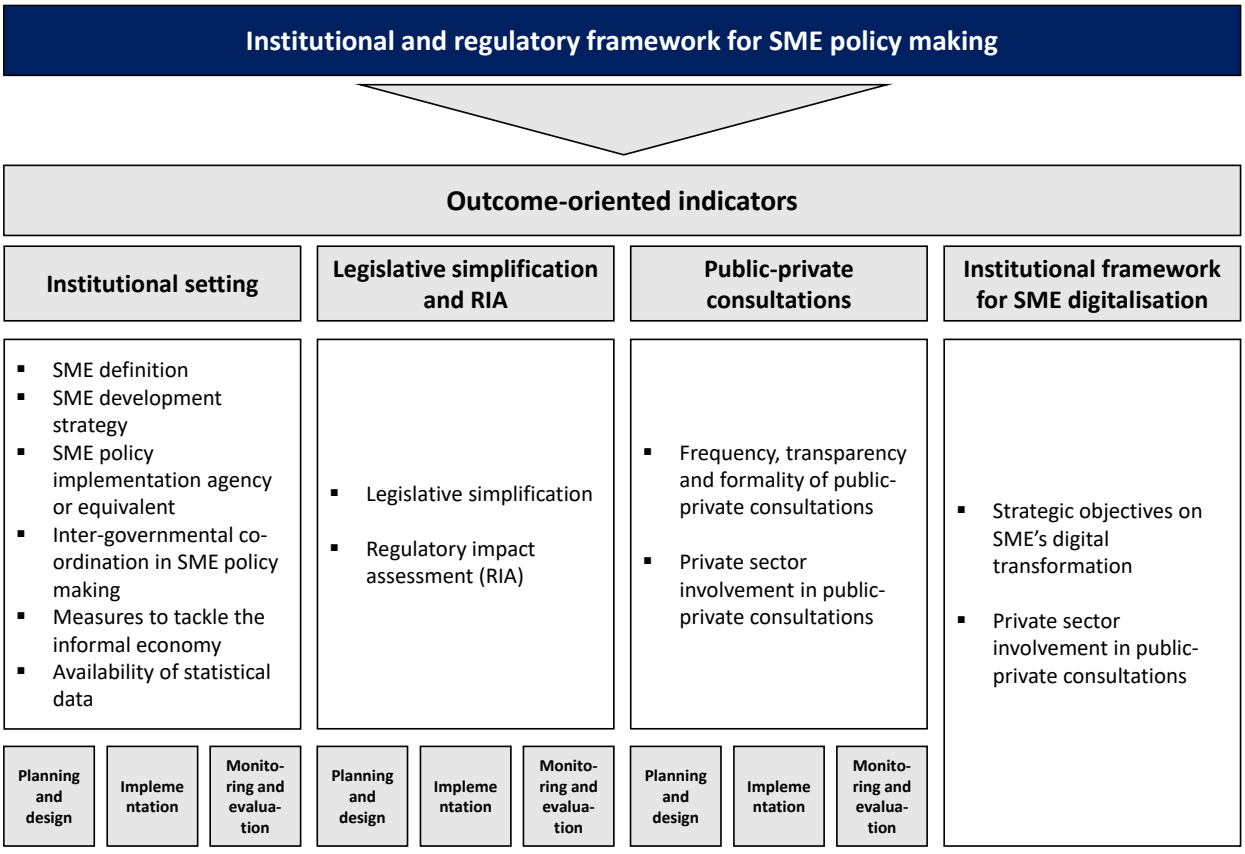
Two important methodological changes have been introduced in this dimension since the previous SBA assessment: i) a new sub-dimension looks at the institutional framework for SME digitalisation, and ii) the analysis considers countries' ability to regularly collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators").

The updated assessment framework considers the following (see Figure 5.1):

- **Institutional setting:** This sub-dimension examines the comprehensiveness and relevance of the framework for SME policy making, including the capacity of institutions in charge of designing and implementing interventions for the SME sector, and mechanisms for inter-institutional co-ordination.

- **Legislative simplification and RIA:** The second sub-dimension looks at the actions taken by the government to reduce the administrative burden on SMEs, focusing on the process of legislative and regulatory simplification and the application of RIA, including the introduction of an SME test to evaluate the impact of new legislative and regulatory acts on small enterprises**.**
- **Public-private consultations:** This involves assessing the frequency, transparency, inclusiveness and formal influence of public-private consultations with a view to ensuring meaningful representation and inclusion of small enterprises in the development of business-related legislation.
- **Institutional framework for SME digitalisation:** This assesses whether and how support for SME digitalisation is embedded in the framework for SME policy making.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information about the following indicators: i) the number of laws/regulations on which RIAs have been conducted, ii) the perception of regulatory quality, iii) the burden of government regulation, and iv) the share of actions/activities implemented as part of the annual SME action plan.

### Figure 5.1. Assessment framework – Institutional and regulatory framework for SME policy msking




## *Analysis*

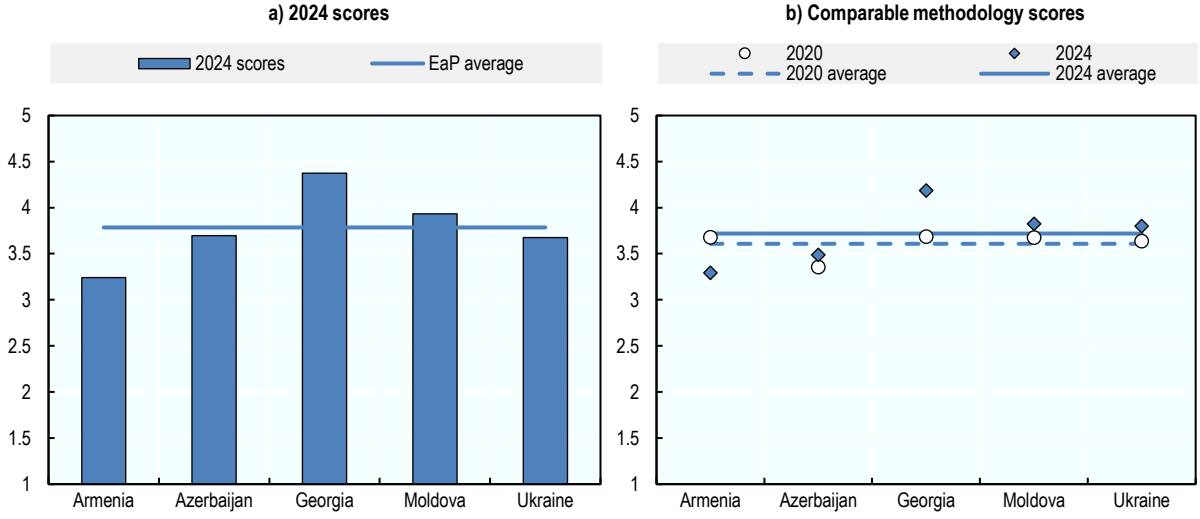
*Regional trend and comparison with 2020 assessment scores*

The EaP region has achieved incremental progress in the dimension covering the SME institutional and regulatory framework since the 2020 assessment. The regional average score for this dimension reached

3.78, reflecting a slight increase in the average country scores (calculated using a comparable methodology) compared to the SME Policy Index 2020. All EaP countries, except for Armenia and Ukraine, recorded incremental improvements in their performance across most of the sub-dimensions, with Georgia confirming its position as top performer.

The overall positive results demonstrate the region's commitment to SME support and business environment reforms during a particularly challenging period. The four years between the end of 2019 and the end of June 2023, the data collection cut-off for the 2024 assessment, featured a series of negative events that have disrupted policy making since the second quarter of 2020. Those events included economic and social turmoil caused by the COVID-19 pandemic and the consequences of Russia's invasion of Ukraine. Policy making returned to its regular course in the third quarter of 2022 across EaP countries, despite significant challenges. Ukraine, in particular, encountered remarkable difficulties due to the war, which to a certain extent impacted Moldova as well.

## Figure 5.2. Institutional and regulatory framework, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/7r0p1h

### *Institutional setting*

The 2020 SME Policy assessment noted that all EaP countries had established the main building blocks of SME policy, based on a clear SME definition, a clear mandate for SME Policy, an elaborated medium-term SME strategy, well-established policy co-ordination and monitoring mechanisms and an operational SME development agency (Table 5.2).

#### SME policy frameworks and strategies

The 2024 assessment confirms that all EaP countries have aligned their national SME definitions to that of the EU in terms of employment parameters. However, the definitions do not align with EU standards in terms of other parameters, i.e. turnover and company assets, as SMEs in EaP economies tend to exist on a smaller scale than in the EU.

## Table 5.2. EaP and EU MSME definitions

| | Micro | Small | Medium | Source |
|---|---|---|---|---|
| EU | < 10 employees<br>≤ EUR 2 million turnover<br>≤ EUR 2 million balance sheet total | < 50 employees<br>≤ EUR 10 million turnover<br>≤ EUR 10 million balance sheet total | < 250 employees<br>≤ EUR 50 million turnover<br>≤ EUR 43 million balance sheet total | European Commission<br>SME definition (europa.eu) |
| Armenia | ≤ 10 employees<br>≤ AMD 100 million turnover<br>(~237 138 EUR) | ≤ 50 employees<br>≤ AMD 500 million turnover<br>(~1 185 690 EUR) | ≤ 250 employees<br>≤ AMD 1500 million turnover<br>(~3 557 070 EUR)<br>≤ AMD 1000 million balance sheet total<br>(~2 371 380 EUR) | Amendments to the Law on State Support of Small and Medium Entrepreneurship<br>arlis.am/documentview.aspx?docID=64617 |
| Azerbaijan | ≤ 10 employees<br>≤ AZN 200 000 turnover<br>(~111 650 EUR) | ≤ 50 employees<br>≤ AZN 3 million turnover<br>(~1 674 747 EUR) | ≤ 250 employees<br>≤ AZN 30 million turnover<br>(~16 747 470 EUR) | Decision of the Cabinet of Ministers of the Republic of Azerbaijan<br>556 - "Mikro, kiçik, orta və iri sahibkarlıq subyektlərinin bölgüsü meyarları"nın təsdiq edilməsi haqqında (e-qanun.az) |
| Georgia | Not defined | < 50 employees<br>≤ GEL 12 million turnover<br>(~4 217 880 EUR) | < 250 employees<br>≤ GEL 60 million turnover<br>(~21 089 400 EUR) | Geostat<br>BS_Methodology_ENG.pdf (geostat.ge) |
| Moldova | < 10 employees<br>≤ MDL 18 million turnover<br>≤ MDL 18 million balance sheet total<br>(~929 185 EUR) | < 50 employees<br>≤ MDL 50 million turnover<br>≤ MDL 50 million balance sheet total<br>(~2 581 070 EUR) | < 250 employees<br>≤ MDL 100 million turnover<br>≤ MDL 100 million balance sheet total<br>(~5 162 140 EUR) | Law No. 179 of 2016<br>lex.justice.md/md/366638/<br>subiect-03-nu-426-me-2022.pdf (gov.md) |
| Ukraine | ≤ 10 employees<br>≤ EUR 2 million turnover | ≤ 50 employees<br>≤ EUR 10 million turnover | ≤ 250 employees<br>≤ EUR 50 million turnover | Commercial Code of Ukraine No. 436-IV<br>The Commercial Code of U... \| on January 16, 2003 № 436-IV (rada.gov.ua) |

Note: Exchange rates as of 28 September, 2023 (Oanda, n.d.[5])

All EaP countries completed the implementation of their respective SME strategies or equivalent strategic documents mentioned in the last SBA assessment, such as Azerbaijan's strategic roadmap for the production of consumer goods at the level of small and medium entrepreneurship. As a positive element, all EaP countries adopted the good practice of conducting an evaluation or at least a review to monitor the progress of their strategy's implementation and used the results to inform the design of a new strategy. In particular, Armenia, Georgia and Moldova conducted independent evaluations, while Ukraine conducted a comprehensive review of its strategy. In Azerbaijan the assessment of the roadmap was conducted by the Center for the Analysis of Economic Reforms and Communications (CAERC).

A new set of mid-term SME development strategies was under elaboration in early 2020 when the COVID-19 epidemic forced EaP countries to prioritise the design and quick implementation of economic emergency measures.

By the end of June 2023, only Georgia had put in place a dedicated medium-term SME Development Strategy for 2021-2025, supported by multi-year action plans. Moldova is completing the approval process for a new National Programme for Promoting Entrepreneurship and Increasing Competitiveness 2023-2026 (PACC 2023-2026) as its strategy elaboration process was delayed by the COVID-19 pandemic and the war in nearby Ukraine. Armenia had approved a new national SME Development Strategy for 2020-2024 in August 2020; while the strategy contains mid-term objectives, its focus was largely on measures designed to respond to the economic crisis generated by the pandemic, and the government is currently considering its review and update.

Azerbaijan opted to include its strategic directions for SME policy within the framework of the new Socio-economic Development Strategy of the Republic of Azerbaijan (2022-2026), specifically under National Priority One: sustainable and growing competitive economy – promotion and sustainable and high economic growth.

In March 2021, Ukraine approved its National Economic Strategy 2030 (NES 2030), a framework document for economic policy, and began developing a new SME Development Strategy. However, after Russia's invasion, the government stopped the strategy elaboration process and decided to focus on short-term action plans responding to the emergencies generated by the war, postponing the elaboration of a new strategy which should then be linked to the recovery and reconstruction plans.

All countries, except Azerbaijan, put effort into estimating the size of the informal economy. In addition, Georgia, Moldova, and Ukraine performed a background analysis on the characteristics of the informal sector. However, only Azerbaijan, Georgia, and Ukraine address the topic in their respective SME policy frameworks.

The new set of mid-term SME development strategies share with the previous strategies the primary objective of improving the operational environment for SMEs and pursuing regulatory reforms. Most of the strategies also include specific sections on supporting SME digital transformation, SMEs' contribution to the green economy, and monitoring and evaluation (M&E).

The focus of all SME strategies in the EaP is on conducting horizontal measures, without selecting specific sectors of activity or segments of the enterprise population. While this approach is consistent with the need to further enhance market dynamics, it does not fully take into consideration new sectors and the emergence of new specializations across the region – for instance in the ICT, tourism, and agri-business sectors, which require the development of supportive ecosystems and call for an integration of different sets of policies, such as those for skills development, trade, infrastructure development and FDI attraction.

The new set of SME strategies should, therefore, explore how to generate synergies with sector/activity-oriented development plans and create opportunities for policy co-ordination with other sets of strategies and the broader national economic development plans.

### SME development agencies

In order to respond to increased demand for SME support, particularly during the COVID-19 pandemic, most EaP countries made significant efforts to increase the operational capacity of their SME development agencies.

In particular, Azerbaijan expanded the network co-ordinated by KOBIA, its SME development agency. This network consists of SME Development Centres operating as both one-stop shops (providing services to entrepreneurs for all types of business activities, including business registration, taxes, licenses, permits and certificates) and 45 SME "friends" operating as KOBIA's local representatives.

Georgia has significantly increased the financial resources allocated to Enterprise Georgia, from GEL 41 million (~EUR 14 million) in 2019 to GEL 291 million (~EUR 100 million)[3], while Moldova in 2022 launched a reform and reorganisation of its SME development agency, now called the Organisation for the Development of Entrepreneurship (ODA), with the aim of improving its governance and simplifying access to SME support programmes.

In 2021, Ukraine transformed its Export Promotion Office into the Entrepreneurship and Export Promotion Office (EEPO) which is now effectively in charge of SME policy implementation as well as export promotion. This is a significant, positive and timely development, as Ukraine has been lacking an SME policy implementation agency that could act as a bridge between the central government and the SME population. EEPO is governed by a supervisory board which includes both the Ministry of Digital Transformation and the Ministry of Economy, and it is providing a valuable channel of communication and assistance with the

enterprise sector. It also manages Diia.Business, the main business portal, which provides online training courses, consultations, and other business support services, in addition to conducting surveys of the enterprise operational conditions at a time of war (see Box 14.4. in the Ukraine country chapter).

The government of Armenia decided to merge the National Center for SME Development (SME DNC) with the Investment Support Center, while also transferring some of the competencies of the SME DNC to the National Center for Innovation and Entrepreneurship, as part of an effort to rationalise and reduce government agencies. The move has caused a temporary disruption in the implementation of SME support programmes, as it involved the closure of the regional network of DNC local offices (there were 10 offices in 2022). This has led to a concentration of the remaining SME development activities in the capital, as well as a reduction of the share of resources allocated to SME support versus investment attraction.

Over the last four years, the SME development agencies in the EaP countries have seen their missions evolve significantly. While they still play a crucial role in promoting entrepreneurship and entrepreneurial skills, they have expanded their activities linked to the provision of targeted business services supporting enterprise growth and digitalisation. In addition, the SME development agencies of Armenia, Georgia and Moldova play an important role as providers of credit guarantees to SMEs, a role that has relevant governance implications.

### Table 5.3. Institutional setting, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.02** | **4.14** | **4.62** | **3.83** | **3.70** | **3.86** |
| Planning & Design | 3.47 | 4.07 | 4.73 | 4.00 | 4.05 | 4.06 |
| Implementation | 2.63 | 4.52 | 4.71 | 3.71 | 3.38 | 3.79 |
| Monitoring & Evaluation | 3.13 | 3.40 | 4.20 | 3.80 | 3.80 | 3.67 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *Legislative and regulatory simplification and RIA application to SME policy*

Legislative and regulatory simplification remains a key priority for all EaP countries, as reflected by a regional average of 3.21. However, their performance in this sub-dimension has somewhat worsened in comparison to the 2020 assessment, except for Georgia.

### Table 5.4. Legislative simplification and RIA, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.03** | **2.90** | **3.50** | **3.35** | **3.27** | **3.21** |
| Planning & Design | 4.13 | 3.40 | 4.53 | 4.00 | 4.20 | 4.05 |
| Implementation | 2.13 | 2.22 | 2.15 | 2.24 | 2.14 | 2.18 |
| Monitoring & Evaluation | 3.13 | 3.53 | 4.73 | 4.73 | 4.20 | 4.07 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

All EaP countries performed strongly on planning and design. This is because all countries have some form of medium-term strategies and action plans for legislative simplification and, with regard to M&E, their monitoring mechanisms have not changed significantly over the last four years. However, their implementation performance has slipped, reflecting the fact that legislative and regulatory simplification

has stalled in recent years. This is largely due to legislative delays stemming from emergencies related to the COVID-19 pandemic and the economic fallout from the war in Ukraine.

Progress in the application of RIA has been equally limited. Table 5.5 presents an overview of the application of RIA in the region.

### Table 5.5. The application of Regulatory Impact Analysis in the EaP countries

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine |
|---|---|---|---|---|---|
| Is there a legal obligation to conduct RIA on business-related legislation? | For major legislative acts | For all legislative acts | | For major legislative acts | For all legislative acts |
| Since when has RIA been formally requested? | 2020 | 2016 | 2020 | 2008 [1] | 2003 [2] |
| Is the institution that proposes legislative acts obliged to conduct RIA? | Yes, for all major legislative acts | Yes, KOBIA and the Ministry of Economy for SME- and business-related legislation | Yes, in case of amendments to existing legislative acts | Yes, for all business-related legislation | Yes |
| Is there a body supervising the RIA applications? | Yes, Department of Regulatory Impact, Prime Minister Office | Yes, Law Service Division of the Presidential Administration | Yes, the Administration of Government of Georgia [3] | Yes, the State Chancellery | Yes, the State Regulatory Service |
| Is there a formal requirement to analyse the impact of new legislation on SMEs? | No, and no formal SME test | Yes, but no formal SME test | Yes, SME test under preparation | Yes, SME test under preparation | Yes, SME test performed |

[1] The methodology was updated in 2019 and is now aligned with EU standards. [2] The methodology was substantially reviewed and improved in 2015. [3] In the case of a legislative initiative by the Government of Georgia, RIA shall be performed by the Parliamentary Secretary of the Government of Georgia.
Source: SBA Assessment questionnaire 2024.

Moldova and Georgia have taken steps to apply RIA systematically to all new primary and secondary legislation and to align their RIA guidelines with international good practices. But while RIA application is well advanced in Moldova, it is not consistently applied in Georgia, partially due to skills gaps at the level of line ministries, lack of effective oversight and the existence of an RIA exemption list.

RIAs are also performed for major legislative acts in Armenia, which introduced new RIA standards in 2019, while in Azerbaijan, regulatory performance assessments using RIA elements are frequently carried out, in particular by the Ministry of Economy and the country's SME Development Agency (KOBIA), for SME and business-related legislation.

In Ukraine, RIA applications are supervised by the State Regulatory Service of Ukraine (SRS), the central body that executes state regulatory policy, and they are systematically performed on major legislative acts. It is worth noting that despite the ongoing invasion, Ukraine has continued to implement its deregulation agenda, completing a relevant number of actions over the last two years. In addition, in January 2023, the government established an Inter-Agency Working Group on deregulation in order to improve deregulation policy co-ordination.

All EaP countries, with the exclusion of Armenia, are formally required to assess the impact of new legislative and regulatory acts on SMEs. To date, however, only Ukraine formally performs an RIA SME test, while Georgia and Moldova are planning to do it in the near future.

*Public-private consultations*

Governments in EaP countries have a relatively well-established practice of conducting open and regular consultations with the private sector. The COVID-19 pandemic – and, in the case of Ukraine, the direct impact of the war – have pushed the governments to make further use of online platforms for public consultations. As a result, EaP countries perform remarkably well in this dimension, resulting in a regional average of 4.15.

Compared with the previous period, it is worth noting that SME representatives were consulted in all EaP countries during the elaboration of the new SME development strategies. It is now a regular practice to conduct public-private consultations prior to the approval of any legislative and regulatory act that has a major impact on SME operations.

The EaP countries have established different channels for consultations. Some focus specifically on SME policy issues, while others are open to the whole private sector. In Georgia, for instance, most SME policy issues are discussed at a session of the Private-Sector Development Advisory Council, while the Deep and Comprehensive Free Trade Agreement (DCFTA) consultative council deals with issues related to the implementation of the EU DCFTA, which has a major influence in guiding the government's trade and regulatory policy. Similarly, Armenia has established an SME Development Council, which is managed by Investment Council (IC) Armenia through its role as Council secretariat. The Council meets on a quarterly basis and is typically chaired by the deputy prime minister (Box 5.1).

In Azerbaijan, the main consultation channel is the Public Council, which is coordinated by the SME development agency, KOBIA. The Ministry of Economy reportedly also conducts ad hoc meetings at sector level. In Moldova, public and private sector representatives meet weekly within the framework of a working group for the regulation of entrepreneurial activities, in addition to ad-hoc meetings held during the elaboration of legislative acts and policy documents.

In Ukraine, most consultations are conducted online through the Diia.Business platform.

All EaP countries require that public consultations are held through public electronic platforms before the approval of new laws during a pre-set time period. In certain cases, the requirement also applies to new regulations. While in some countries the platforms are managed centrally (see the e-draft.am platform in Armenia, the particip.gov.md platform in Moldova, and the ichange.gov.ge platform in Georgia), in Azerbaijan and Ukraine legislative acts are posted for consultation on the website of the responsible ministry. However, data on the usage of online consultation platforms and the responses by public institutions are limited and fragmented, so it is difficult to assess the use and effectiveness of online consultations.

### Table 5.6. Public-private consultations, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **4.16** | **3.40** | **4.65** | **4.27** | **4.26** | **4.15** |
| Frequency and transparency of PPCs | 4.33 | 3.11 | 4.67 | 4.50 | 4.42 | 4.20 |
| Private sector involvement in PPCs | 4.07 | 3.40 | 4.96 | 3.67 | 4.73 | 4.16 |
| Monitoring and evaluation | 4.00 | 4.00 | 4.00 | 5.00 | 3.00 | 4.00 |

Note: PCCs = public-private consultations. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### Box 5.1. Armenia's SME Development Council

In 2007, the European Bank for Reconstruction and Development (EBRD) initiated the establishment of Investment Councils (ICs) in its countries of operation to facilitate collaboration between governments and the private sector, with the aim of improving the investment climate. IC Armenia and its SME Development Council were created in 2012 through a joint initiative of the Government of Armenia and the EBRD. Initially supported by the EBRD, since 2020 it has been funded by the UK Government's Good Governance Fund (GGF).

The operations of the SME Development Council in Armenia encompass a public-private dialogue platform, connecting the Armenian government with SME associations to foster the development of business oriented legislative reforms. This includes two types of meetings:

- *Monthly sub-council meetings,* led by the Minister of Economy, involving preliminary discussion of the identified issues and provision of proposals.
- *Quarterly council meetings,* led by the deputy prime minister, and including the IC Armenia experts, to identify legislative bottlenecks hindering the smooth operation of **SMEs** in Armenia and to work closely with the respective ministries to develop reform packages targeted at **bettering the business environment** and investment climate in Armenia.

The Sub-Council consists of 11 members, including representatives from NGOs, business associations, and foundations as well as from the Ministry of Economy, State Revenue Committee, and Ministry of Finance. The Council includes additional members such as the head of the EBRD Resident Office in Armenia, the ambassador of the United Kingdom to Armenia, the deputy prime minister, and relevant state body ministers.

Over the past 10 years, the SME Development Council led by the IC Armenia team has achieved 25 large-scale legislative reforms, including preferential tax regimes for IT start-ups, the introduction of a sales tax, and leasing reforms. Since 2012, there have been 18 Council meetings, 5 of them chaired by Armenia's Minister of Economy. The monthly Sub-Council meetings propose an average of 7-10 changes to SME-regulating legislation.

Source: (SME Development Council, 2023[6])

#### *Institutional framework for SME digitalisation*

This sub-dimension, included for the first time in the 2024 assessment, includes a number of indicators covering the use of electronic government platforms, the presence of strategic directions supporting the digital transformation of SMEs and their consistency with the overall SME development strategy, the role played by SME development and other public agencies in this domain as well as the monitoring of digital transformation initiatives.

The assessment results indicate that EaP countries perform well in this area, achieving an average score of 4.14.

All EaP countries have started taking SME digitalisation into consideration in their institutional and policy frameworks for SMEs. They are progressively integrating some related provisions in key policy documents (e.g., the National Digital Strategy in Armenia; existing or upcoming SME development strategies in Azerbaijan, Georgia, and Moldova). In terms of institutional settings, Georgia and Moldova have given a clear mandate and allocated resources to their SME development agencies to implement measures / programmes in the field. Azerbaijan is also investing significant resources and has established an

Innovation and Digital Development Agency under the Ministry of Digital Development and Transport. As for Ukraine, the country has made digital transformation of the public administration, the productive sector, and the whole society a central objective and placed all actions under the co-ordination of a dedicated Ministry of Digital Transformation, while the Diia.Business platform has proved to be a very flexible and effective tool for communicating and providing services to the enterprise sector.

All EaP countries have shown a significant commitment to providing public support to accelerate the digital transformation; however, the measures implemented so far have been predominantly focused on fostering digital / IT start-ups, and have paid less attention to the digital transformation of entrepreneurs in non-IT sectors for instance. Moreover, the resources allocated to this objective in most EaP countries remain relatively limited.

### Table 5.7. Institutional framework for SME digitalisation, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.50** | **4.05** | **4.54** | **4.20** | **4.40** | **4.14** |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### *The way forward*

- The new set of strategic documents on SME development should **take into consideration the structural changes that occurred in the SME population** due to the economic crisis generated by the COVID-19 pandemic. Revisions of the strategic documents should be conducted when necessary.
- All EaP countries should **take elaborate shorter-term action plans to secure the strategy implementation**. Ukraine could consider elaborating its next SME Development Strategy once the situation in the country normalises, but it could already establish a task force to develop plans for supporting the enterprise sector, including SMEs, in the reconstruction phase. Meanwhile, Ukraine should continue with the implementation of short-term action plan to deal with the emergencies caused by the war.
- All EaP countries should consider how to 1) **generate synergies between their SME development strategies and sector/activity-oriented development plans** and 2) **develop more advanced instruments of policy co-ordination** with other sets of strategies (local development, skill development and digitalisation) and the broader national economic development plans.
- Much progress has been achieved over the last four years in improving the operational capability of the region's SME development agencies. All EaP countries should follow the good practice of Moldova by **upgrading the governance mechanisms of their SME agencies**, and – particularly for those agencies that are also active in the provision of credit guarantees – increase their operational autonomy and set clear reporting lines to their respective supervising ministries.
- **RIA should be applied systematically to all new legislative and regulatory acts** that are expected to have a significant impact on the business sector in all EaP countries, and the potential impact on small-scale enterprises should be evaluated through the RIA SME tests.
- All EaP countries should **ensure that public-private consultations (PPCs) are open to representatives of different classes and types of SMEs and that the voices of enterprises operating in new emerging sectors** (e.g. ICT firms, agri-bio enterprises, small tourist operators and logistics firms) are heard and considered. Following the good practice introduced by Ukraine

with the Diia.Business platforms, EaP countries should expand the use of electronic platforms to consult with the enterprise sector and conduct regular business surveys.

- EaP countries should **establish dedicated programmes designed to support the digital transformation of SMEs** associated with sufficient human and financial resources, as well as measurable targets.

## Operational environment for SMEs

Throughout their life cycles, businesses constantly need to interact with public institutions, physically or digitally, to carry out necessary procedures such as registering a company, obtaining a business licence, and filing and paying taxes.

Inadequate government services, lengthy and costly procedures, and onerous regulatory requirements can impose excessive burdens on businesses, potentially resulting in the loss of viable firms. SMEs are particularly affected, as they often operate on thin profit margins, so the resulting increased costs may force some to cease their operations (OECD, 2020[1]). By contrast, reducing the burdensome procedures for starting and managing businesses, as well as simplifying interactions with public authorities, enables SMEs to allocated limited resources to innovative activities or job creation (Parker and Kirkpatrick, 2012[7]), thereby leading to more-dynamic market entry and efficiency gains.

Against this backdrop, it is important that public administrations are responsive to SME needs, as prescribed by principle 4 of the Small Business Act (European Commission, 2008[3]). To this end, the provision of government services through digital platforms improves reach and efficiency and plays an important role in reducing corruption and informal economic activity, given the increased transparency, objectiveness and enforceability of decisions. The move to a one-stop, automated, web-enabled registry capable of delivering online products and services with authenticated users and documents represents global best practice. Further measures to promote business-friendly administrative procedures can include the application of the silence-is-consent principle as well as unification of identification numbers and enhanced data exchange across all government agencies. SMEs can also benefit from streamlined and tailored tax schemes because simplification provisions encourage business creation and reduce the burden of tax compliance, while also reducing tax collection costs.

### *Assessment framework*

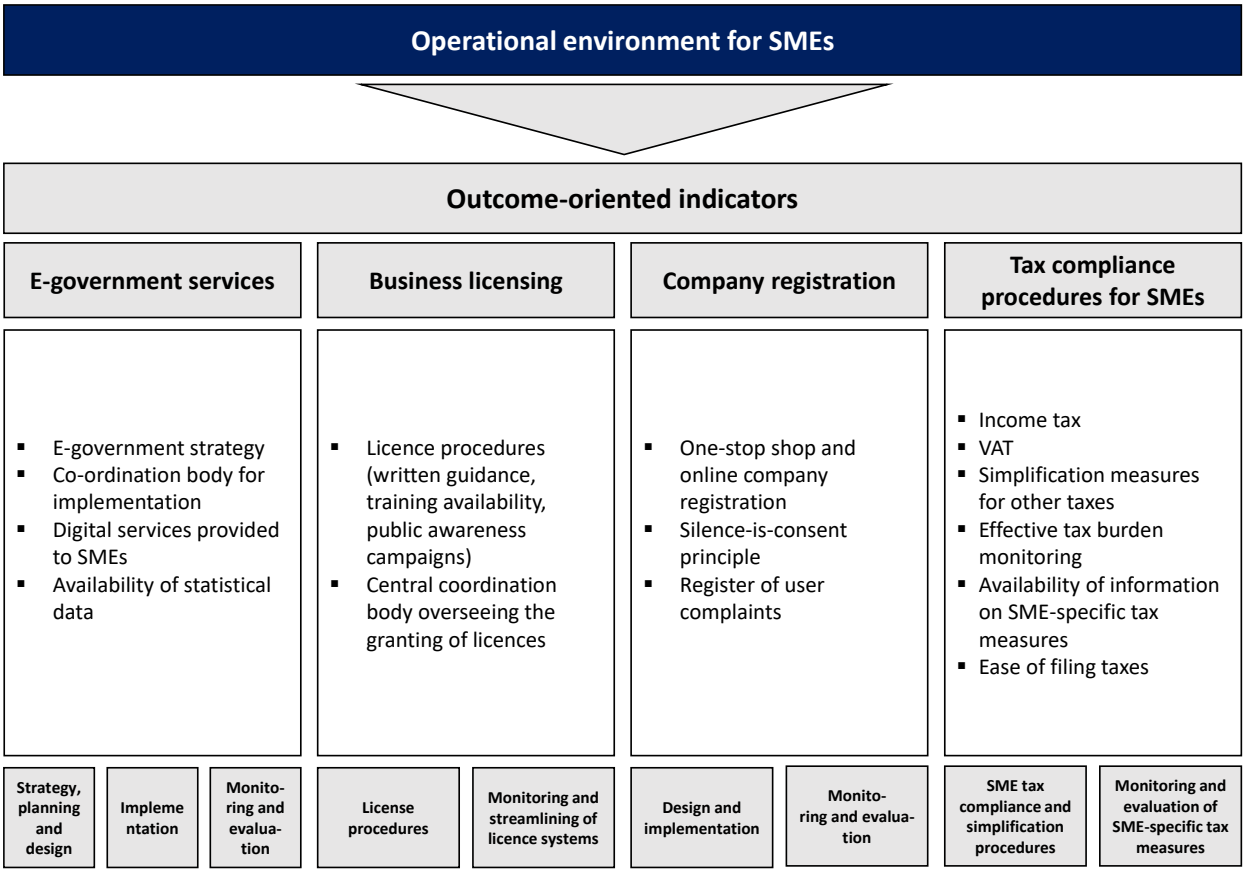
Two important methodological changes have been introduced in this dimension since the previous SBA assessment. First, all indicators from the World Bank's Doing Business report – previously used to evaluate the effectiveness of company registration procedures and the ease of filing taxes – are no longer considered due to the discontinuation of the exercise. Second, the analysis now considers countries' ability to regularly collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators").

The updated assessment framework considers the following (see Figure 5.3):

- **E-government services:** This sub-dimension assesses government's strategies for providing e-services, the range of services provided, the level of inter-operability among the different data banks run by the public administration, and the actions taken to implement an open-data approach.
- **Company registration:** The second sub-dimension, which focuses on the procedures necessary to register a company, includes indicators looking at the presence of one-stop shops and the introduction of single company identification numbers.

- **Business licencing:** This subsection analyses the actions taken by governments to reduce the number of required business licenses and permits and to improve the business license allocation systems, through better co-ordination among the licensing institutions.
- **Tax compliance procedures for SMEs:** The last sub-dimension assesses policies designed to simplify SMEs' tax compliance, considering special tax regimes and incentives.
- The new section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information for the following indicators: i) number of enterprises (by enterprise size class); ii) persons employed (by enterprise size class); iii) value added (by enterprise size class); iv) turnover (by enterprise size class); v) number or share of high-growth enterprises; vi) enterprise birth rate / business creation; vii) enterprise survival rate in first, second, third, fourth and fifth years of operation; viii) number of days required to obtain a company registration certificate; and ix) number of administrative steps required to obtain a company registration certificate.

### Figure 5.3. Assessment framework – Operational environment for SMEs



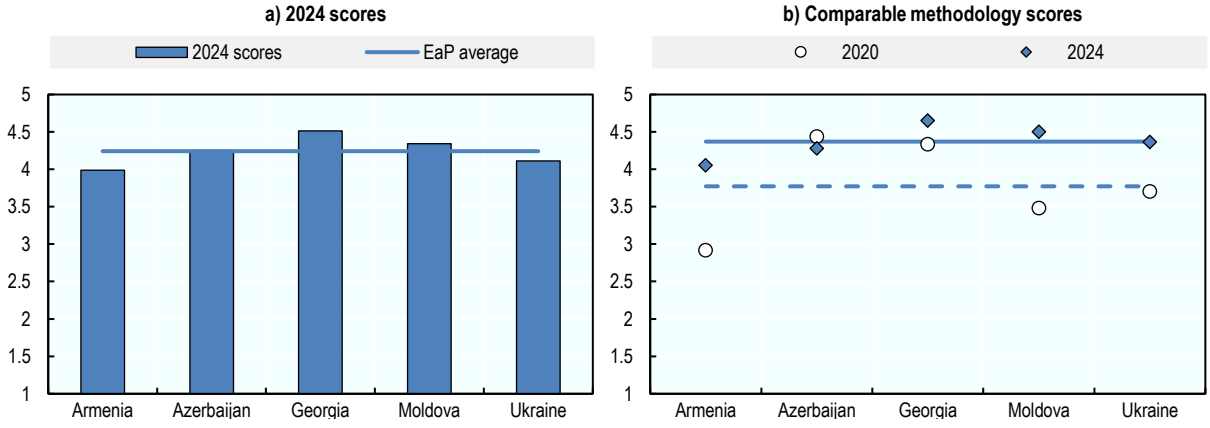

## *Analysis*

*Regional trend and comparison with 2020 assessment scores*

All EaP countries are deeply committed to cultivating a more favourable and supportive business environment for SMEs. This commitment has led to the recognition of enhancing the operational conditions for SMEs as a major policy priority.

The 2024 assessment confirms the good results obtained in this dimension, with the average EaP score reaching 4.24. Comparison with 2020 results is difficult, as the indicators applied to the sub-dimensions dealing with company registration and tax compliance procedures have substantially changed. The overall picture confirms that Georgia has moved furthest towards international good practices concerning the SME operational environment. Armenia and Moldova have improved their performance; Azerbaijan's score has remained substantially stable; and Ukraine, which was lagging behind in the 2020 EaP dimension average, has significantly improved its position.

## Figure 5.4. Operational environment for SMEs, dimension scores




Note: CM = comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/wmuof0

### *E-government services*

All EaP countries have made substantial progress in the sub-dimension related to the provision of e-government services, with the EaP average score reaching 4.31.

All countries have significantly increased the range of e-government services available through e-government platforms, simplified service accessibility and improved e-governance. The only area where progress has been relatively limited is M&E, as data on the use of e-government services by SMEs (especially data broken down by enterprise type and location) are relatively scarce. Better data availability could lead to more-targeted information campaigns and training for SMEs, further improving e-government utilisation rates.

All EaP countries currently have approved multi-year strategic documents guiding the expansion of e-government services. This may be a document dealing with public administration reform, as in case of the Public Service Development Strategy 2022-2025 adopted by Georgia in 2021, or a specific e-government strategy, as in the case of Armenia's National Digitalisation Strategy and the Digital Azerbaijan project conducted by the E-Government Development Center.

The principle leading the transition towards e-government is "digital first and digital by default" – meaning that digital services cover, to the extent possible, the entire range of government services, while access to e-government services is made so easy that it becomes the preferred access route (although an alternative route is always available).

Each EaP country has also established, or is currently establishing, a single platform or access portal for e-government services. The Diia platform in Ukraine (see Box 14.4 in the Ukraine country chapter) is

considered the most advanced tool in this regard, providing a wide range of e-services accessible throughout the country and to the Ukrainian diaspora abroad. E-government platforms are also operational in Armenia, Georgia and Moldova (which launch its MDelivery document delivery platform in 2022). Azerbaijan has developed a portal called the Azerbaijani Service and Assessment Network, or ASAN (asan.gov.az), which provides access to a wide range of services to the population, and is also working to bring all business services, which are currently accessible only through the websites of each administration, under a common platform.

### Table 5.8. Map of the e-Government Service available in the EaP countries

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine |
|---|---|---|---|---|---|
| Filing taxes and social contributions | Fully digital | Fully digital | Fully digital | Fully digital | Fully digital |
| Contributions to the pension funds | Fully digital | Fully digital | Fully digital | Fully digital | Fully digital |
| Services related to the cadastre | Fully digital | Partially digital | Fully digital | Fully digital | Fully digital |
| Issuing/obtaining business certificates, attestations, excerpts, and copies of acts | Partially digital | Fully digital | Fully digital | Fully digital | Partially digital |
| Applications to state support programs for SMEs | Partially digital | Partially digital | Fully digital | Partially digital | Partially digital |
| Reporting data to the statistical agency | Fully digital | Fully digital | Fully digital | Fully digital | Fully digital |

Source: SBA Assessment questionnaire 2024.

The “only once” principle, which implies that a user’s data are automatically exchanged among public institutions and are not requested each time a user makes an enquiry, is only partially applied across the region due to issues related to the inter-operability of public sector data banks. Only in Georgia does this principle appear to be consistently applied.

Also, the practice of collecting data on the use of e-government services by SMEs and conducting enquires about the satisfaction of e-government service users is not systematically applied.

### Table 5.9. E-government services, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **4.00** | **4.25** | **4.29** | **4.34** | **4.66** | **4.31** |
| Strategy, planning & design | 3.93 | 4.30 | 4.92 | 4.82 | 4.56 | 4.51 |
| Implementation | 4.21 | 4.33 | 4.36 | 4.42 | 4.88 | 4.44 |
| Monitoring & Evaluation | 3.67 | 4.00 | 3.00 | 3.33 | 4.33 | 3.67 |

Note: See the “Policy framework, structure of the report and assessment process” chapter and Annex A for information on the assessment methodology.

#### *Company registration*

Company registration procedures are relatively simple, fast and inexpensive in all EaP countries. The 2020 assessment already had recognised substantial progress made by the EaP countries in this sub-dimension. Over the last four years, while no major changes have been recorded, online registration capacity has been further expanded and company registration fees have been reduced in some countries. The 2024 EaP average is 4.73, and all EaP countries have recorded scores for this sub-dimension above 4.00. While the 2024 assessment indicates that there has been incremental progress in this area, a direct comparison with the 2020 scores is not possible since the 2020 scores were based largely on data from the World Bank’s Doing Business report, now discontinued.

Georgia and Armenia have confirmed their position as leaders in this area. Company registration in these two countries can be performed entirely online (through a single act) and released in a few minutes, and

new enterprises are given a single registration number valid for interactions with all public administration bodies.

Ukraine and Azerbaijan have also simplified company registration procedures. In Azerbaijan, this is part of the government's efforts to improve the country's position on rankings made by international organisations and research institutes. Company registration can be conducted online and in Ukraine the entire procedure can be completed in about in three days. Azerbaijan, Moldova and Ukraine have abolished public fees for company registrations.

### Table 5.10. Company registration, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **4.88** | **4.52** | **5.00** | **4.74** | **4.52** | **4.73** |
| Design & implementation | 4.80 | 4.20 | 5.00 | 4.90 | 4.20 | 4.62 |
| Monitoring & evaluation | 5.00 | 5.00 | 5.00 | 4.50 | 5.00 | 4.90 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *Business licencing*

The reduction in the number of compulsory business licenses and the simplification of business license application procedures have been long-term objectives of regulatory reform in all EaP countries. The EaP countries have continued to improve in this regard, achieving a regional average score of 4.34. Notably, all countries recorded significant progress, particularly in the reduction of license requirements and the simplification and transparency of license-granting procedures.

All EaP countries have established an online portal for handling most license applications. In Moldova, the online platform covers 86% of all license applications and operates as a one-stop shop. Similarly, in Georgia most license applications can be made online and the "silence is consent" principle is applied. Ukraine approved a new Law on Licenses in 2019 and has put a legal limit to the value of license fees. Azerbaijan has reviewed the number of compulsory licenses and reduced the licenses fees by 50%, with a further 50% reduction for applicants located in less developed areas. Armenia is also operating a central online platform for license applications, but it has slightly increased the number of compulsory licenses to cover activities that present public safety risks.

### Table 5.11. Business licencing, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.66** | **3.96** | **5.00** | **4.69** | **4.40** | **4.34** |
| Licence procedures | 4.14 | 4.43 | 5.00 | 4.43 | 4.83 | 4.57 |
| Monitoring & streamlining of licence systems | 3.33 | 3.64 | 5.00 | 4.87 | 4.11 | 4.19 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *Tax compliance procedures for SMEs*

For this 2024 assessment, the structure of this sub-dimension has been radically changed from that adopted for the 2020 assessment. While the previous structure focused mainly on tax compliance procedures and the administrative tax burden on SMEs, using data from the now-discontinued World Bank Doing Business report, the new structure analyses the main characteristics of each country's tax regime

for enterprises and individual entrepreneurs, as well as the actions taken by the national tax administration to monitor the tax burden on SMEs and individual entrepreneurs and evaluate the effective tax rates imposed on those groups of tax payers. Therefore, the 2020 scores and the 2024 scores for this sub-dimension should be compared with caution.

Starting in the second quarter of 2020, to counteract the negative impact of the COVID-19 epidemic on enterprise business activity and stimulate economic recovery, all the EaP countries introduced a number of temporary tax measures – a mix of tax exemptions, tax payment delays and accelerated depreciation rates – aimed at easing the tax burden on the enterprise sector, targeting in particular the sub-sectors most affected by the pandemic. Most those emergency measures have now been phased out, starting from the end of 2022.

The overall results of the 2024 assessment show that all EaP countries have established a relatively light and well-balanced tax regime for SMEs, although gaps are recorded in the area of the systematic monitoring of the tax burden and the calculation of the effective tax rates on SMEs, as well as the administration of VAT refunds in a number of EaP countries. The 2024 EaP average is 3.44, with Georgia being the only country to record an average sub-dimension score higher than 4.00.

All EaP countries have introduced simplified tax regimes for individual entrepreneurs and small-scale enterprises. In all EaP countries – with the exception of Azerbaijan, where the special regime applies only to individual entrepreneurs – these two categories of economic entities can opt for a non-VAT taxpayer regime and are subject to an average turnover tax varying from 1% in Georgia to 5% in Armenia. The standard corporate income tax rate is set at 20% in Armenia, Azerbaijan and Georgia; at 18% in Ukraine; and at 12% in Moldova. In Ukraine a temporary surcharge of 2% was introduced in 2022 to finance the cost of the war.

Some EaP countries have introduced tax incentives for specific enterprise types. This is the case in Azerbaijan, which covers the enterprises qualified as “start-ups” by KOBIA as well as “cluster enterprises” and in Moldova, which applies a highly reduced tax regime to enterprises located in ICT parks.

All EaP countries have also introduced measures to reduce the administrative burden associated with tax declarations and tax payments. All countries have established online tax and VAT declaration systems, but only Georgia and Moldova have introduced automatic VAT refund systems for all enterprise categories. The tax administration system in Ukraine is still relatively complex, in terms of the number of tax regimes and the number of taxes applied to enterprises and individual entrepreneurs.

All EaP countries are making efforts to improve the monitoring of tax regimes and the evaluation of effective tax rates. For instance, Azerbaijan and Moldova have started to evaluate the effective tax burden on SMEs, while Georgia and Moldova undertake regular evaluations of measures aimed at easing tax compliance for SMEs.

### Table 5.12. Tax compliance procedures for SMEs, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **2.73** | **3.70** | **4.26** | **3.78** | **2.73** | **3.44** |
| Tax compliance & simplification procedures | 3.12 | 3.59 | 4.53 | 3.35 | 3.12 | 3.54 |
| M&E of SME-specific tax measures | 2.14 | 3.86 | 3.86 | 4.43 | 2.14 | 3.29 |

Note: M&E = monitoring and evaluation. See the “Policy framework, structure of the report and assessment process” chapter and Annex A for information on the assessment methodology.

### *The way forward*

- The EaP countries should **systematically collect data on the use of e-government services by different categories of SME** (by size, type of ownership and location) to i) identify the type of enterprises that encounter more difficulties in accessing and using e-government services and ii) map the use of e-government service by SMEs. This would allow public agencies to improve the design of e-government services and to conduct promotional campaigns and training sessions targeting SMEs with lower e-government service utilisation rates.
- Company registration procedures in EaP countries are among the most advanced. However, all EaP countries should **continue to monitor their performance** in this area, for instance by measuring time, costs and administrative steps required and monitoring the performance of their registration agencies.
- All EaP countries should **calculate the effective tax rate applied to different categories of SMEs and evaluate the impact of special tax regimes and incentives** targeting individual entrepreneurs and small enterprises in order to avoid potential distorting effects and disincentives to enterprise growth.
- **Automatic VAT-refund systems should be put in place in all the EaP countries** (currently only Georgia and Moldova have developed such a system). All countries should act to minimise the potential for fraud and misuse by applying risk-assessment techniques.

## Bankruptcy and second chance

Business failure, as much as business creation, is part of a dynamic, healthy market. Well-designed insolvency and restructuring procedures ensure that viable firms are restructured, while unviable firms are liquidated, so as to ensure that productive assets remain in use and scarce resources are allocated efficiently (IMF, 1999[8]). On the other hand, inefficient, lengthy and burdensome proceedings represent additional costs for both creditors and debtors (OECD et al., 2020[9]). In this context, efficient and predictable insolvency regimes can improve the allocation of capital and labour in the economy, thereby increasing productivity and output (Diez et al., 2021[10]). In addition, as efficient insolvency laws are one of the key criteria investors use to decide whether to invest across borders, increasing confidence in cross-border financing can boost capital markets (European Commission, 2020[11]).

Timely identification and resolution of financial difficulties are also pivotal elements of a comprehensive framework as they can prevent bankruptcy altogether, thus effectively lowering the rate of bankruptcy and optimising the value of assets that creditors can recover (Garrido, 2012[12]; European Commission, 2011[13]). Relevant measures include early-warning mechanisms to facilitate early detection of financial distress (e.g. alert mechanisms triggered by non-payment of taxes or social security contributions) (European Parliament, 2019[14]), as well as advisory services (such as debt counselling) and information tools (such as self-test websites) provided to businesses fearing failure. When designed and implemented properly, similar measures can help SMEs identify and overcome financial challenges, maintain continuity, and continue contributing to the economy. Furthermore, in accordance with Principle 2 of the Small Business Act, it is important to “ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance” (European Commission, 2008[3]) by implementing initiatives to reduce the cultural stigma surrounding entrepreneurs’ failure, and by providing failed entrepreneurs with the tools necessary to re-enter the market.

### *Assessment framework*

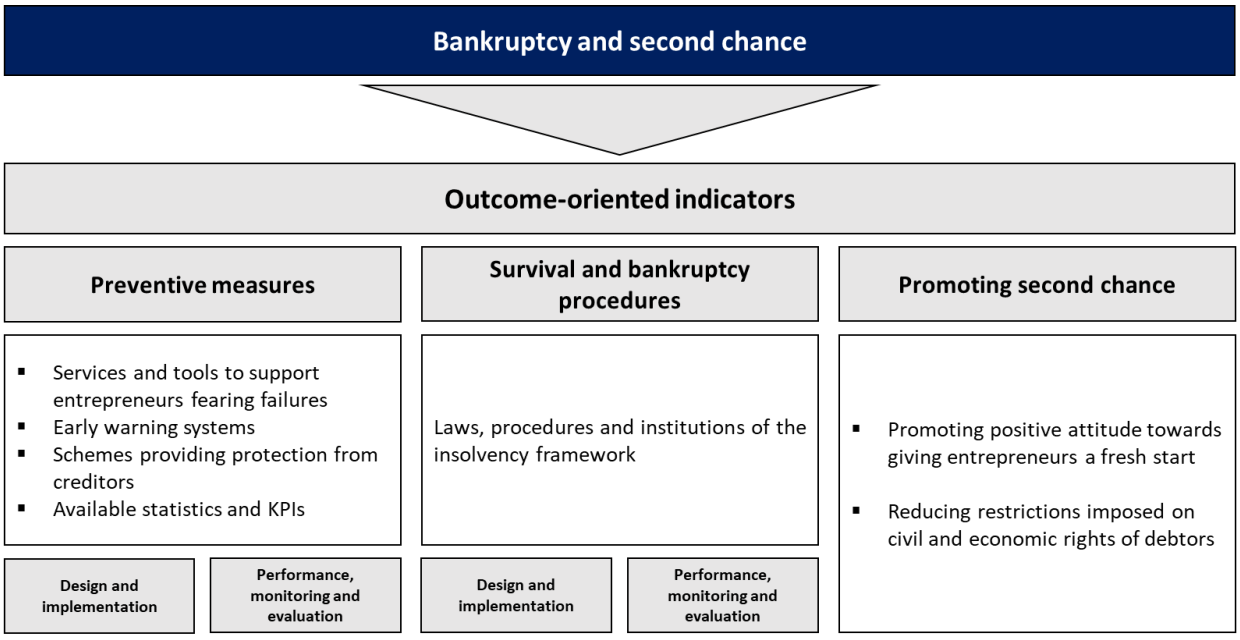
This dimension assesses the extent to which EaP countries are facilitating market exit and re-entry for businesses by adopting effective and efficient frameworks to prevent and face insolvency, as well as to re-start businesses after bankruptcy.

Three important methodological changes have been introduced in this dimension since the previous SBA assessment: i) a new thematic block has been introduced to investigate performance, monitoring, and evaluation of policies to prevent insolvency; ii) all indicators from the World Bank's Doing Business report previously examined to assess performance, monitoring and evaluation of insolvency frameworks are no longer considered due to the discontinuation of the exercise; and finally, iii) the analysis now considers countries' ability regularly to collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators").

The assessment framework considers the following (see Figure 5.5):

- **Preventive measures:** This sub-dimension looks at the design, implementation and monitoring of measures designed to prevent insolvency, including early-warning mechanisms to facilitate early detection of financial distress. It also examines the advisory services and information tools (such as debt counselling and self-test websites) provided to businesses fearing failure.
- **Survival and bankruptcy procedures:** Here, the design, implementation and monitoring of insolvency regimes in EaP countries is assessed, looking at how relevant laws and procedures align with international best practice.
- **Promoting second chance:** This sub-dimension examines the extent to which EaP countries facilitate re-entry in the market of failed but honest entrepreneurs seeking a fresh start.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information about the following indicators: i) number of bankruptcies (by enterprise size class), ii) share of insolvency procedures that result in rehabilitation rather than liquidation of the enterprise, iii) average time required by insolvency proceedings, iv) average cost of insolvency proceedings (as a percentage of the estate), v) recovery rate (in cents on the dollar), vi) average time required to obtain full discharge from bankruptcy, and vii) the share of second-chance entrepreneurs among all active entrepreneurs.

## Figure 5.5. Assessment framework – Bankruptcy and second chance

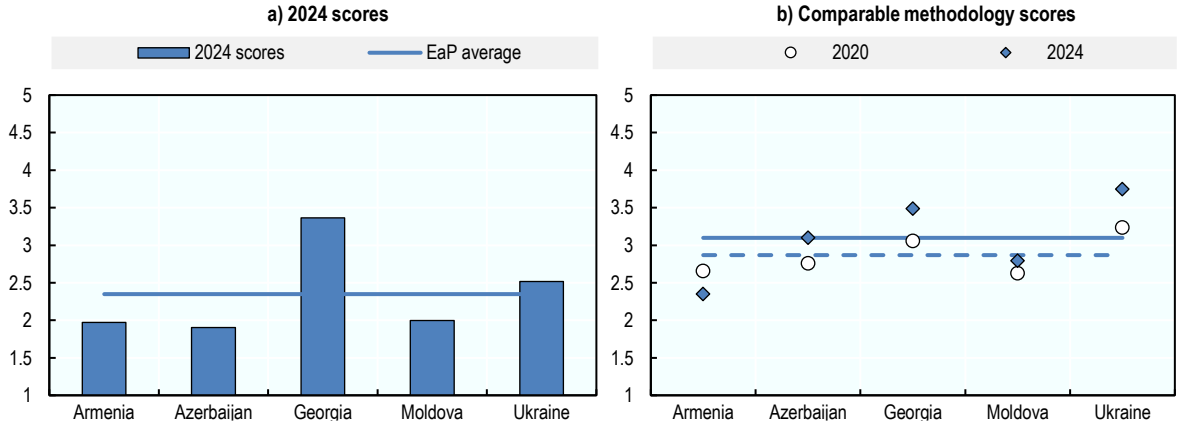



### *Analysis*

*Regional trend and comparison with 2020 assessment scores*

Uneven progress has been achieved in the field of *Bankruptcy and second chance* with respect to the previous SBA assessment, with EaP countries proceeding at different paces across the different sub-dimensions. Overall, all countries improved their performance with respect to the 2020 assessment, except for Armenia. However, this dimension remains one of the weakest performance areas across the EaP region, with an average score of 2.35 (see Figure 5.6), which indicates substantial scope for improvement. This outcome can largely be attributed to EaP countries' weak frameworks for preventing bankruptcy and their limited efforts to promote second chance for failed but honest entrepreneurs.

## Figure 5.6. Bankruptcy and second chance, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### *Preventive measures*

This sub-dimension looks at measures in place to prevent insolvency. Timely identification and resolution of financial difficulties can effectively lower the rate of bankruptcy and optimise the value of assets that creditors can recover (Garrido, 2012[12]; European Commission, 2011[13]). Relevant measures include early warning mechanisms to facilitate early detection of financial distress (e.g. alert mechanisms triggered by non-payment of taxes or social security contributions) (European Parliament, 2019[14]), as well as advisory services (such as debt counselling) and information tools (such as self-test websites) provided to businesses fearing failure. When designed and implemented properly, similar measures can help SMEs identify and overcome financial challenges, maintain continuity, and continue contributing to the economy.

All EaP countries show significant room for improvement in their measures to identify financial distress and prevent insolvency. This clearly emerges from the sub-dimension scores (Table 5.13), which average 1.90. It is important to mention that the scores are also negatively affected by the introduction of a new thematic block that assesses efforts to monitor and evaluate existing measures to prevent insolvency - an area in which all countries, except Georgia, underperform.

In all EaP countries, except Armenia, businesses in financial distress can access information on available government support, as well as training courses for entrepreneurs fearing failure; and in Azerbaijan, Georgia and Ukraine they can seek advice via dedicated websites or call centres. Georgian SMEs experiencing financial difficulties can access advisory services and generic guidance through the web guide businessguide.ebrd.ge, developed by the EBRD in partnership with Enterprise Georgia and the Rural Development Agency. Additionally, in Moldova, ODA's staff has been trained on the topic of early-warning systems, and such mechanisms have been applied to some companies on a trial basis. In 2021, through the implementation of the DanubeChance2.0 project, ODA carried out several activities related to the elaboration of a national early warning mechanism. However, the project has expired and, although there is a proposal for a new Second Chance Programme for SMEs, it has not yet been approved.

**Table 5.13. Preventive measures, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **1.34** | **1.69** | **3.24** | **1.46** | **1.75** | **1.90** |
| Design & implementation | 1.86 | 2.71 | 3.60 | 2.14 | 2.89 | 2.64 |
| Performance, monitoring & evaluation | 1.00 | 1.00 | 3.00 | 1.00 | 1.00 | 1.40 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Unfortunately, despite the above-mentioned initiatives, information on tools and support available to SMEs often lacks visibility and accessibility. Even though both public and private institutions offer services to SMEs in financial distress, they often fail to advertise them effectively. Moreover, well-developed and comprehensive early-warning systems that can detect circumstances that could potentially lead to insolvency[4] are not yet in place in any of the countries. Box 5.2 (below) discusses the evolution of early warning systems in Europe, and Box 5.3 (at the end of the chapter) presents an example of an early warning tool. Finally, most of the EaP countries have yet to develop systems to monitor existing measures for preventing insolvency. The only exception is Georgia, where the insolvency reform, including initiatives to prevent bankruptcy, has been monitored and evaluated under the project ReforMeter, a reform-tracking tool supported by the USAID Economic Governance Program and implemented by the ISET Policy Institute.[5]

### Box 5.2. Early-warning systems in European Commission Directive 2019/1023

**European Directive on restructuring and insolvency**

The adoption of Directive 2019/1023 on restructuring and insolvency signifies a pivotal achievement in the development of European insolvency law and was the culmination of complex negotiations. Before this, in 2014 the European Commission issued Recommendation 2014/135/EU, which discussed substantive insolvency matters, such as the need to ensure a second chance for honest entrepreneurs and establish restructuring procedures outside the scope of formal insolvency proceedings. The final text of the Directive was adopted in 2019 and set minimum standards in various areas related to restructuring and insolvency.

**Design of early-warning systems**

Early-warning systems are one of the main building blocks of Directive 2019/1023. They can act as a **self-assessment tool entrepreneurs** can use to assess their economic situation and financial performance, and are particularly useful for SMEs, which usually lack in-house analytics. Such systems can be implemented in numerous ways and have varying degrees of sophistication. A simple tool could be represented by a software application on a public website where entrepreneurs can input relevant data and obtain a preliminary diagnostic. More advanced early-warning systems can go beyond mere self-assessment and detection and **trigger an intervention mechanism**, e.g. by automatically involving an auditor when a concrete financial risk is identified.

Two additional elements are key to design an effective early warning system:

- *Identification of well-defined indicators*. These indicators should serve as triggers, signalling potential economic issues within the enterprise. For instance, they could include a combination of financial ratios that assess factors such as liquidity, profitability, efficiency and viability, as well as leverage, among others.*
- *Integration with insolvency and debt restructuring mechanisms*. The early warning system should be connected to insolvency and debt restructuring processes. This connection can take various forms, from sending alert messages to entrepreneurs in financial distress to mandating insolvency or preventive restructuring proceedings if corrective actions are not taken promptly. It is essential to ensure that this integration always respects the confidentiality of sensitive financial information, which is vital to prevent entrepreneurs from being disincentivized to use the early warning systems.

* These ratios are respectively working capital / total assets, retained earnings / total assets, earnings before interest and taxes / total assets, and debt/earnings ratio.
Source: (Garrido et al., 2021[15])

*Survival and bankruptcy procedures*

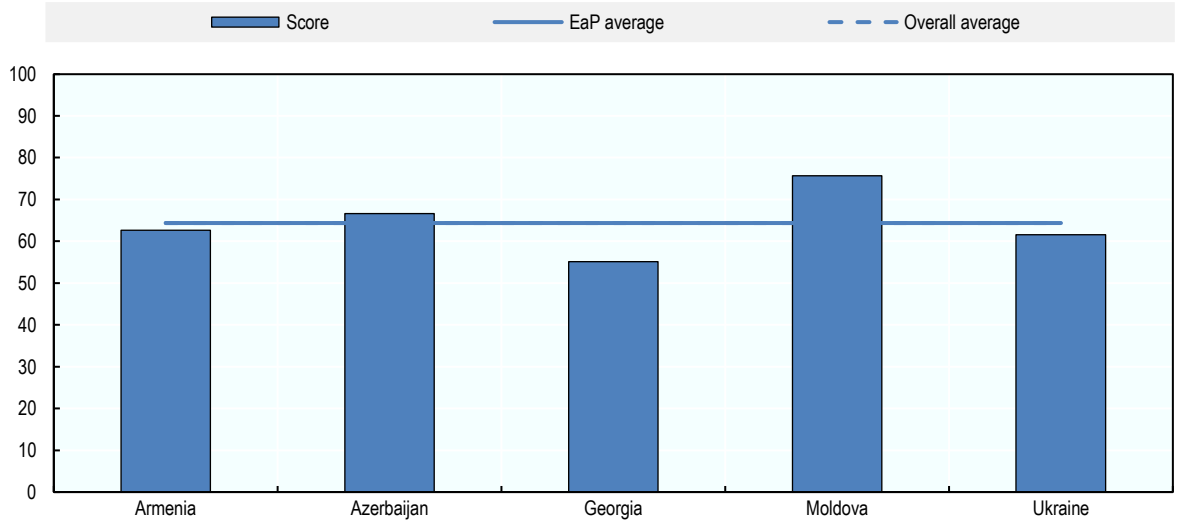
This sub-dimension assesses the design, implementation and monitoring of insolvency regimes in EaP countries, looking at how relevant laws and procedures align with international good practice. Analysed aspects include the existence of laws or other procedures on distressed companies, receivership and bankruptcy, the provision of out-of-court restructuring as a less-costly alternative to formal bankruptcy proceedings, and the existence of simplified reorganisation procedures for smaller firms. In addition, this sub-dimension assesses the scope and structure of the monitoring and evaluation system.

EaP countries have fairly well-designed bankruptcy frameworks, achieving an average score of 3.03, (Table 5.14). The scores in this sub-dimension, however, are negatively affected by changes to the assessment methodology.

Somewhat positive results also emerge from the EBRD Business Reorganisation Assessment (EBRD, 2021[16]), which monitored insolvency policies and practices during the COVID-19 crisis. The assessment, conducted through a questionnaire, was carried out to provide the EBRD, its economies of operations and investors with an up-to-date overview of business reorganisation tools and to propose areas where further development of national legislation is needed. According to the results of this study, EaP countries perform, on average, at the same level as other assessed countries (Figure 5.7), with a particularly solid performance in the area of "General Approach to Corporate Reorganisation"[6]. It is important to note, however, that this assessment does not take into account reforms implemented after the cut-off date (7 November 2020), and that the results for Georgia are based on previous legislation that was in force in 2020.

## Figure 5.7. EBRD Business Reorganisation Assessment (2020)

Overall assessment results, by EaP country




Note: The scale goes from 0 to 100, where 100 represents best performance. The assessment considers insolvency frameworks only as they were at the cut-off date of 7 November 2020. In particular, results for Georgia are based on the previous legislation in force in 2020.
Source: OECD calculations based on EBRD (2021[16]), *Business Reorganisation Assessment*.

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Since 2020, all countries, except Ukraine, have amended their legislative frameworks for bankruptcy, resulting in important improvements. In Armenia, the amendments led to the establishment of a self-regulatory association of practitioners and to the introduction of the electronic exchange of documents between all parties involved in a proceeding. In Azerbaijan, issues regarding the grounds for insolvency and the voting rights of the creditors on the recovery plan were clarified, and regulations on court hearings were introduced. In Moldova, significant improvements were made with the introduction of a simplified bankruptcy procedure and the establishment of an electronic registry for insolvency cases. Finally, in Georgia, the adoption of a new law significantly transformed and improved the insolvency regime, shifting the focus from liquidation to rehabilitation.

Since the last assessment, Georgia and Moldova have introduced out-of-court settlements, which are now available in all EaP countries, except in Armenia. The availability of such simplified procedures and the existence of specialised commercial or insolvency courts in all countries (with the exception of Moldova), have improved the efficiency and speed of insolvency regimes. On the other hand, although insolvency registers are available in all countries except Azerbaijan, aggregated data on insolvency cases is not available. Finally, abbreviated or simplified procedures for small cases or SMEs are available only in Georgia and Moldova.

### Table 5.14. Survival and bankruptcy procedures, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **2.74** | **2.15** | **4.13** | **2.72** | **3.39** | **3.03** |
| Design & implementation | 3.35 | 3.88 | 4.33 | 3.80 | 3.96 | 3.87 |
| Performance, monitoring & evaluation | 2.33 | 1.00 | 4.00 | 2.00 | 3.00 | 2.47 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Despite these positive elements, substantial room for improvement remains. In particular, Armenia, Azerbaijan and Ukraine should consider the introduction of simplified or pre-packaged proceedings specifically targeting small cases and/or SMEs.[7] These mechanisms should provide for shorter timelines and fewer formal requirements, allowing for time- and cost-efficient reorganisation of SME debtors. Moreover, all EaP countries should direct more effort into monitoring and evaluating insolvency procedures, developing comprehensive mechanisms to increase the efficiency and effectiveness of bankruptcy frameworks. Finally, countries should collect and make available more comprehensive and systematic data on insolvency and efficiency of procedures.

#### *Promoting second chance*

This sub-dimension assesses the extent to which insolvency regimes promote a "fresh start" for honest entrepreneurs going bankrupt and reduce the stigma associated with a failing business. Second chance can be assimilated to the treatment of failed entrepreneurs, once the bankruptcy procedures are completed.[8] The promotion of second chance creates incentives for entrepreneurship and experimentation by increasing firms' entry and by allowing entrepreneurs to apply their experience and lessons learnt to new businesses (OECD, 2018[17]).

EaP countries register their worst performance in this sub-dimension, with a regional average score of 1.50. In fact, none of the five countries has an overall national strategy or a comprehensive policy framework for promoting second chance for entrepreneurs seeking a fresh start after bankruptcy. Moldova formerly led in this regard, with ODIMM (now ODA) previously involved in the DanubeChance2.0 project, which gave formally bankrupt entrepreneurs a second chance in the Danube Region through awareness campaigns, training, and restructuring services; however, the project expired in June 2021. Georgia offers some training opportunities to failed entrepreneurs, but these are not done systematically, and are oriented more toward supporting entrepreneurs' efforts to recover in the aftermath of the crisis generated by the COVID pandemic. On a positive note, in most countries (Azerbaijan, Georgia and Ukraine) there are no restrictions imposed on bankrupt entrepreneurs that might prevent them from re-entering the market.

### Table 5.15. Promoting second chance, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **1.00** | **1.33** | **2.33** | **1.00** | **1.83** | **1.50** |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

All EaP countries would benefit from adopting initiatives to promote a second chance for bankrupt entrepreneurs. Even when there are no formal barriers preventing bankrupt entrepreneurs from starting fresh, there often are no explicit incentives, dedicated strategies or information campaigns or relevant programmes to promote the rehabilitation of honest entrepreneurs and reduce the cultural stigma surrounding business failure.

### *The way forward*

- All EaP countries should **establish well-developed and comprehensive early-warning systems for systematic detection of insolvency**, with the objective of preventing bankruptcy. Early-warning systems should be based on both financial and non-financial variables and should deliver as an outcome tailored recommendations and practical advice on overcoming the identified issues (see Box 5.3). Armenia, in particular, should introduce pre-insolvency tools, such as training and debt counselling by practitioners at local level, for entrepreneurs in financial distress.
- Armenia, Azerbaijan, and Ukraine should **introduce simplified or pre-packaged proceedings specifically targeting small cases or SMEs**. Simplified insolvency processes with fewer formalities, shorter deadlines and lower costs may be beneficial for smaller businesses and can be supplemented with practical online documentation templates and checklists. The law should set out clear eligibility criteria that identify which businesses should benefit from any simplified arrangements (EBRD, 2022[18]) (see Box 5.4). Armenia could further improve its bankruptcy framework by introducing out-of-court debt restructuring procedures as a less costly alternative to formal bankruptcy proceedings.
- All EaP countries should **adopt a co-ordinated and proactive second-chance strategy** to facilitate a fresh start for honest entrepreneurs. Key features of second-chance promotion could include facilitated access to finance after bankruptcy, guidelines or training for re-starters, and awareness-raising campaigns. Georgia should ensure the continuation of existing training on how to start fresh beyond the context of the COVID-19 pandemic. Moreover, Armenia and Moldova should remove all barriers and restrictions imposed on failed entrepreneurs that might prevent or hinder them from re-entering the market.
- Armenia, Azerbaijan, Moldova and Ukraine should direct efforts towards **developing a comprehensive mechanism to monitor and evaluate insolvency procedures as well as programmes to prevent insolvency**, so as to increase their efficiency and effectiveness.
- Finally, all EaP countries should **collect more comprehensive and systematic data on SME insolvency and efficiency of procedures** – such as the number of bankruptcies, the share of insolvency procedures that result in rehabilitation rather than liquidation, the average time needed to obtain full discharge from bankruptcy, and the share of second-chance entrepreneurs.

### Box 5.3. Early detection of crisis symptoms: the *Alert Procedure* in the Italian Code of Corporate Crisis and Insolvency

In 2022, Italy adopted a new "Code of Corporate Crisis and Insolvency" which deeply reformed the Italian legal framework for business crisis and insolvency. The Code, which transposes EU directive 2019/1023, establishes a so-called "alert procedure" (AP), which can be considered as an early warning tool to promptly identify the symptoms of a crisis and appropriate measures for overcoming it.

The code identifies as relevant crisis symptoms the following:

- payroll liabilities overdue for at least 30 days amounting to more than half of the total monthly payroll liabilities;
- liabilities vis-à-vis suppliers overdue for at least 90 days in an amount exceeding the amount of non-overdue liabilities;
- exposures vis-à-vis banks and intermediaries overdue for more than 60 days amounting to at least 5% of exposures, and
- payment delays that trigger the reporting obligations of so-called "qualified public creditors"

In the presence of any of these symptoms, the company's supervisory bodies and qualified creditors are obliged to notify the management body of the existence of crisis symptoms and set a reasonable timeframe for management to report on potential initiatives and action taken in this regard. Should the management fail to provide an adequate response the newly established competent body for crisis management must be notified. If the state of crisis is confirmed by a panel of experts, viable measures aimed at overcoming the crisis are devised and can be implemented without the need to inform or involve the creditors.

Source: (Engage, 2022[19]), (Clifford Chance, 2022[20]), (INSOL Europe, 2022[21]).

### Box 5.4. Australia's Small Business Restructuring Process

Introduced by the Australian Federal Government in 2021, the Small Business Restructuring Process is a new formal insolvency appointment designed to aid small businesses in resolving financial distress. Under this restructuring process, company directors and management maintain control under the guidance of a restructuring practitioner. Its primary objective is to grant directors and the company an opportunity to propose a plan to creditors for repaying their debts, either in full or in part, within a period not exceeding three years.

The Process begins with the company's directors appointing a restructuring practitioner who assesses the business' eligibility for the Process and assists in developing a restructuring plan. The plan allows the company to repay creditors and operates under a fixed remuneration proposal for a specific period. The company has 20 business days to propose the plan to creditors, during which a moratorium on security enforcement is in effect. Creditors then have 15 business days to vote on the plan, and it requires support from over 50% in value of unrelated creditors to be approved. If approved, the company continues trading under director control while the plan is administered. Once the plan's terms are satisfied, the company is released from its admissible debts. If not approved, the company does not automatically enter other insolvency processes, and directors and creditors may consider alternative options.

In summary, the Small Business Restructuring Process is designed to assist financially distressed small businesses by allowing directors to propose a plan to repay creditors, providing better outcomes for stakeholders. It offers a structured approach to managing insolvency and aims to preserve business continuity while addressing financial difficulties.

Source: (SV Partners, 2023[22])

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## Notes

[1] "The definition of the "Think Small First" principle implies that policy makers give full consideration to SMEs at the early policy development stage. Ideally, rules that affect business should be created from the SMEs' point of view – or, in other words, SMEs should be considered by public authorities as being their "prime customers" as far as business regulation is concerned. The principle relies on the fact that "one size does not fit all" and a lighter-touch approach can also be beneficial to larger businesses. Conversely, rules and procedures designed for large companies create disproportionate, if not unbearable, burdens for SMEs as they lack the economies of scale (European Commission, 2009[23]).

[2] The SME Test implements the "Think Small First" principle through: i) preliminary assessment of businesses likely to be affected, ii) consultation with SMEs and SME representative organisations, iii) measurement of the impact on SMEs (cost-benefit analysis), and iv) use of mitigating measures, if appropriate. The European Commission is committed to a systematic and proportionate application of the SME Test in its impact assessment guidelines. The updated SME test is presented in the Better Regulation toolbox, revised in July 2017. See https://single-market-economy.ec.europa.eu/smes/sme-strategy/sme-test_en.

[3] Data received from the Government of Georgia, as part of the responses to the SBA assessment questionnaire

[4] According to Directive (EU) 2019/1023, similar early-warning tools may include alert mechanisms when the debtor has not made certain types of payments, as well as incentives under national law for third parties with relevant information about the debtor (such as accountants and tax and social security authorities) to flag to the debtor a negative development.

[5] https://reformeter.iset-pi.ge/en.

[6] The assessment evaluated countries' performance in five key areas, which largely follow the sequential steps that businesses take when faced with financial distress and when they embark on a reorganisation exercise: 1) General Approach to Corporate Reorganisation, 2) Planning and Initial Stage of the Reorganisation, 3) The Reorganisation Plan, 4) The Reorganisation Approval Phase, and 5) Other Relevant Aspects. For more information see https://ebrd-restructuring.com/storage/uploads/documents/1.pdf.

[7] A few examples of such mechanisms are Kosovo's fully-fledged reorganisation procedure specifically tailored to SMEs, and Hungary' simplified preventive restructuring procedure for SMEs. In addition, even in the absence of separate specific proceedings, a few other economies (such as North Macedonia and Slovenia) include less-burdensome requirements for smaller companies (EBRD, 2022[24]).

[8] Promotion of second chance should hence be distinguished from restructuring/survival measures for financially distressed businesses.

# 6 Pillar B – Entrepreneurial Human Capital

This pillar assesses the progress made by the five Eastern Partner countries in building entrepreneurial human capital in terms of 1) entrepreneurial learning and women's entrepreneurship and 2) SME skills. After introducing the assessment framework, the chapter presents the results of the analysis for entrepreneurial learning policies and institutional arrangements, looking at both formal education and lifelong learning, and measures for women entrepreneurs, including policy frameworks, women-specific support services, and gender-sensitive data collection, among others. The second part of the assessment delves into SME skills development, focusing on the provision of training services for SMEs as well as skills intelligence and its use for policy and practice. Each of these sub-dimensions concludes with a set of policy recommendations to help EaP countries overcome persisting challenges.

## Introduction

Human capital – which can be defined as the knowledge, skills and other personal characteristics embodied in people that help them to be productive – is a key driver of firm growth and productivity. The latter is positively correlated with the entrepreneur's years of schooling, while several studies suggest that human capital plays a role in enterprises' growth and overall survival (Shen et al., 2021[1]; Queiró, 2022[2]). It can be enhanced by, among other things, entrepreneurial learning, i.e. the promotion of an entrepreneurial mindset and behaviour through educational programmes, training and non-formal learning (European Training Foundation, 2018[3]). Research has shown that entrepreneurial learning has a significant influence on entrepreneurship, and notably business performance. The topic has been gaining increasing attention and relevance against the backdrop of recent social, economic and political shocks, including the COVID pandemic and Russia's war of aggression against Ukraine, as individuals and firms have found themselves forced to adapt to new realities, transition to digital solutions, and come up with innovative ways to tackle rising challenges. The existence of an entrepreneurial mindset, combined with a diversified skillset, fosters adaptability, resilience and innovation.

The multifaceted nature of the topic calls for comprehensive and adaptive policies. The European Union (EU) is providing guidance and direction to promote entrepreneurship in its Member States, most recently through its New Skills Agenda (European Commission, 2021[4]). Building on the ten actions of the European Commission's 2016 Skills Agenda, this new strategy re-emphasises the need to promote entrepreneurial mindsets and relevant skills to enhance competitiveness, improve resilience and ensure social fairness. In 2016 the EU had launched the European Entrepreneurship Competence Framework (EntreComp) in 2016 (Bacigalupo et al., 2016[5]), which identifies fifteen competences in three key areas, encompassing both hard and soft skills, such as creativity, opportunity-spotting, financial and economic literacy, stakeholder engagement, initiative-taking, planning and management. It provides a reference framework for policy makers for the design of formal education and lifelong learning opportunities. Indeed, these competences need to be developed at all stages of life – from the education system to continuous learning in adulthood.

When developing policy approaches to build entrepreneurial human capital, policy makers should include SME-specific measures. SMEs often face more difficulties than larger firms when dealing with skills shortages, particularly when trying to attract and retain skilled workers – which impedes profitability and growth prospects. Compared to larger firms, SMEs also have fewer resources for providing upskilling and reskilling opportunities to their employees. These issues are widespread across countries, including in the EaP region – the lack of an adequately educated workforce is among the main obstacles faced by SMEs, according to the EBRD-EIB-World Bank Business Environment and Enterprise Performance Surveys (BEEPS) (World Bank, 2021[6]). Government support for SME skills development is therefore essential to overcome financial and educational barriers, and to encourage firms to address the challenges of digitalisation and sustainability. It also helps them adjust to the swift evolution of skills demand, prompted by rapidly changing economic and labour market conditions.

The entrepreneurial human capital dimensions are at the core of the economic and SME development agenda, and policies addressed under Pillar B cut across all dimensions of the Small Business Act. Adequate skills and competences are not only key enabling factors for entrepreneurial activity, business innovation and internationalisation, but also help SMEs make economic performance more sustainable through greening and digitalisation. This results in synergies within the SBA framework: for instance, adequate skills and competences should be fostered by SME support services; green skills underpin strategies for sustainable development and resource efficiency; financial literacy is essential for SMEs' access to capital; and digital skills are a pre-requisite for a successful digital transformation, including approaches to e-commerce.

This chapter analyses the state of policies developed in EaP countries to help citizens acquire and develop entrepreneurial skills and competences, in line with EU policy frameworks for human capital and SME development. It assesses the extent to which entrepreneurial learning, women's entrepreneurship, and

SME skills are developed through policy design, implementation, and monitoring and evaluation – with increased granularity compared to the last SBA assessment, and with additional attention given to stakeholder co-ordination and impact evaluation.

This chapter will address the two dimensions of Pillar B: i) entrepreneurial learning and women's entrepreneurship and ii) SME skills.

### Table 6.1. Pillar B: Country scores, by dimension and sub-dimension (2024)

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average 2024 | *EaP average 2024 (CM)* | *EaP average 2020 (CM)* |
|---|---|---|---|---|---|---|---|---|
| **Entrepreneurial learning/women's entrepreneurship** | **2.91** | **3.07** | **4.17** | **4.09** | **3.95** | **3.64** | ***4.22*** | ***3.81*** |
| Entrepreneurial learning | 3.10 | 2.88 | 3.87 | 4.14 | 4.01 | 3.60 | *4.26* | *3.67* |
| Women's entrepreneurship | 2.50 | 3.71 | 4.90 | 4.40 | 4.21 | 3.94 | *4.16* | *4.03* |
| Outcome-oriented indicators | 3.29 | 1.86 | 3.29 | 2.71 | 2.71 | 2.77 | - | - |
| **SME skills** | **2.37** | **3.59** | **4.12** | **3.89** | **3.91** | **3.57** | ***3.78*** | ***2.97*** |
| SME skills | 2.41 | 3.76 | 4.25 | 4.10 | 4.01 | 3.71 | *3.78* | *2.97* |
| Outcome-oriented indicators | 2.00 | 2.00 | 3.00 | 2.00 | 3.00 | 2.40 | - | - |

Note: CM = comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Entrepreneurial learning and women's entrepreneurship

The central concept behind entrepreneurial learning under the Small Business Act for Europe is the idea of entrepreneurship itself – enabled by cognitive and behavioural skills such as opportunity spotting, risk assessment, teamwork, and mobilising resources – as a key competence. Efforts to develop entrepreneurship are often grouped into three different approaches – namely, teaching about entrepreneurship (theoretical approach to the topic), teaching for entrepreneurship (occupationally oriented method to provide necessary skills and competences) and teaching through entrepreneurship (process-based approaches, embedding entrepreneurship in other subjects in general education (Lackéus, 2015[7]). Practical entrepreneurial experience is essential in this regard, but is often challenged by resource constraints, such as time, budget and skills. Strong connection between schools and businesses is also needed to create opportunities for real-life practical experiences.

To be effective, entrepreneurial learning requires a comprehensive policy approach that combines both formal and non-formal learning. While education systems should include and teach entrepreneurship as a key competence across national curricula, these skills can be further developed through lifelong learning opportunities (e.g. hackathons, bootcamps), thereby increasing employability and helping tackle skills mismatches by allowing for a more well-rounded and well-developed workforce (Bell, 2016[8]).

A major obstacle to ensuring equal female labour market participation is persisting gender gaps in entrepreneurial activities. These gaps cost economies in terms of missed opportunities for ideas, innovation and job creation (OECD, 2023[9]). In OECD countries, women are on average 30% less likely than men to be launching or running a new business, and they are also less likely to create employment opportunities for others. Women also often operate different types of businesses than men – they are, for instance, under-represented in the ICT sector, and were more negatively affected by the COVID-19 pandemic due to their concentration in the hardest-hit sectors, such as high-contact service industries. Moreover, women tend to have different motivations and intentions than men in their entrepreneurial undertakings, with some starting a business to avoid the "glass ceiling" in regular employment. Common

to OECD, EU and EaP countries, these gender gaps in the quantity and quality of entrepreneurial activities derive from a variety of factors – such as skills gaps (e.g. in business and risk management or opportunity recognition), uneven access to finance and weaker networks. Understanding and addressing the needs of women entrepreneurs and promoting equal opportunities across countries and sectors are therefore critical to bridging the gaps and unlocking women's full entrepreneurial potential, thereby contributing to more sustainable and diversified economies.

### *Assessment framework*

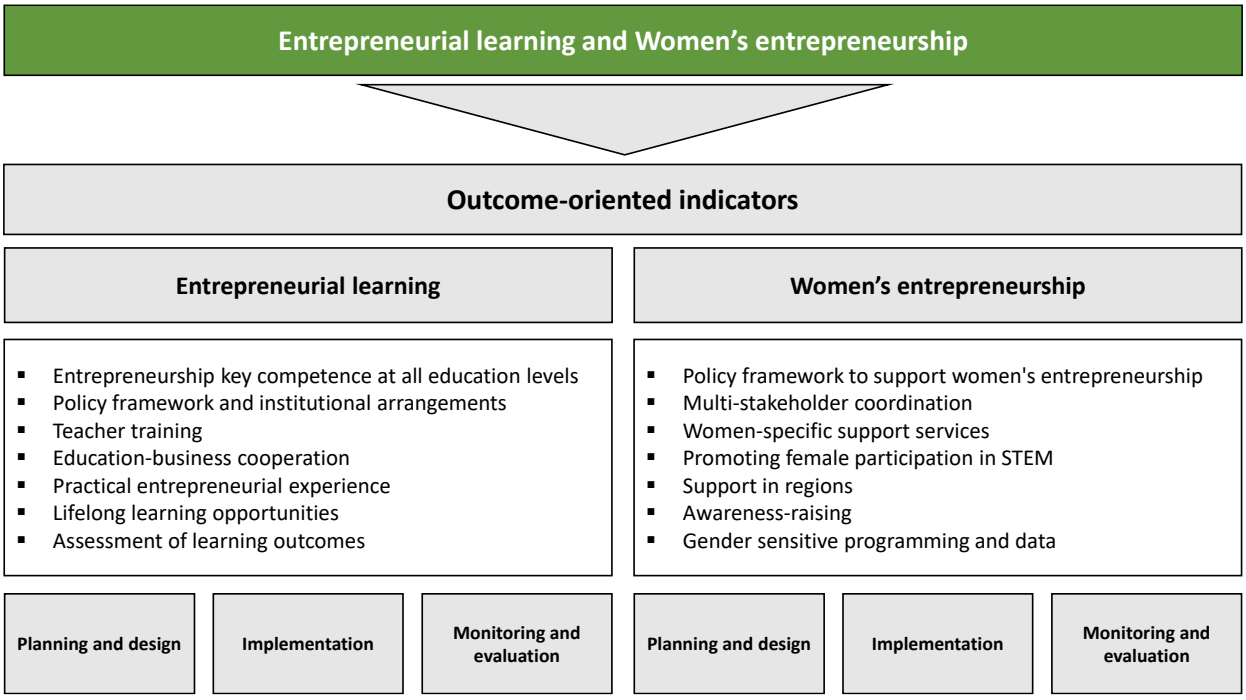
This dimension assesses EaP countries' progress in i) fostering entrepreneurial learning through formal school education and lifelong learning initiatives and ii) promoting women's entrepreneurship.

Two important methodological changes have been introduced in this dimension since the previous SBA assessment: first, the analytical framework has been enhanced, with additional questions (emphasising policy implementation, monitoring and evaluation) designed to increase the granularity of this assessment. Second, the analysis now considers countries' ability to regularly collect quantitative information to monitor the impact of policies on target groups (students, teachers, women) and on entrepreneurship ("outcome-oriented indicators").

As a result, the assessment framework for this dimension is composed of the following:

- **Entrepreneurial learning:** This sub-dimension focuses on the policy context and institutional arrangements for entrepreneurship across all levels of education (primary, lower and secondary (general and vocational), and higher) and on lifelong learning initiatives. This new assessment round places more emphasis on policy implementation (e.g., the existence of a dedicated budget and targets) for each level of education, and pays particular attention to policy impact, notably learning outcomes, and to monitoring and evaluation practices.
- **Women's entrepreneurship:** The second sub-dimension assesses the policy framework and measures implemented to support women business owners and efforts undertaken to bridge the gender gap in entrepreneurial activities. This sub-dimension has benefitted from new insights into women-specific programmes and a new focus on measures to encourage women's participation in science, technology, engineering and mathematics (STEM) disciplines, and to promote women's entrepreneurship outside the capital city. Greater consideration is also given to co-ordination across stakeholders and to addressing remaining barriers to women's entrepreneurship.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information about the following indicators: i) share of students in formal education engaged in entrepreneurial learning programmes, by level of education; ii) share of teachers in formal education trained in entrepreneurship key competence development, by level of education; iii) entrepreneurship education in primary and secondary schools and iv) in higher education (the extent to which training in creating and managing SMEs is incorporated within the education and training system); v) the share of young people having acquired at least one practical entrepreneurial experience prior to leaving school; vi) perception of entrepreneurship as a desirable career choice; vii) employment rate of graduates from vocational education programmes in the first year after graduation; viii) incidence of self-employment, within the general population, by education level, ix) women, by educational attainment, x) men, by educational attainment; xi) established business ownership rates, by sex; xii) newly established enterprises, by sex of the owner; xiii) share of women participants in SME support programmes; and xiv) value of collateral needed for a loan, by sex of loan applicant.

### Figure 6.1. Assessment framework – Entrepreneurial learning and Women's Entrepreneurship

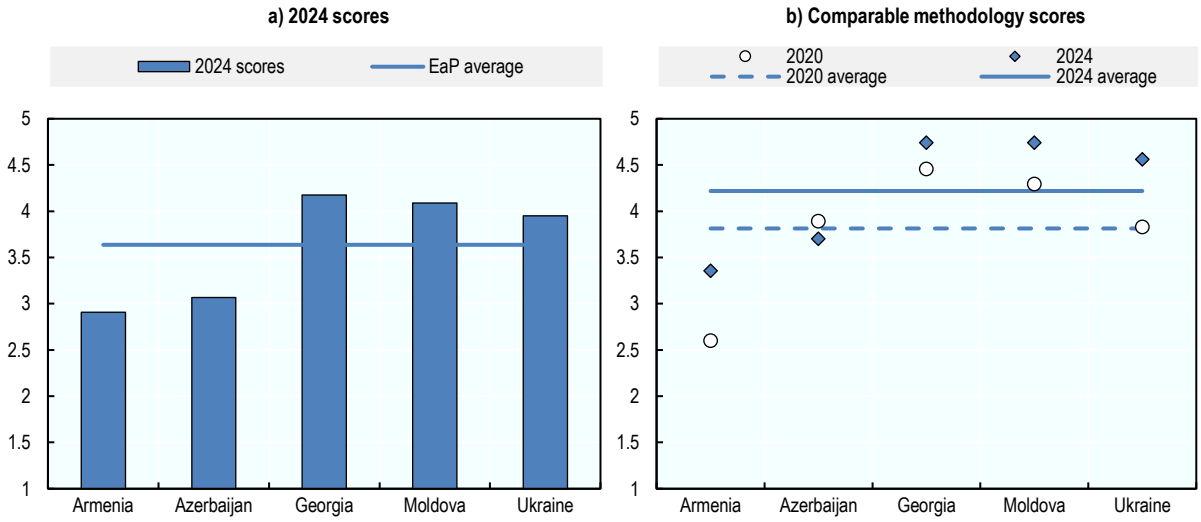



## *Analysis*

*Regional trends and comparison with 2020 assessment scores*

Starting from a strong basis in the last SBA assessment, EaP countries have been working to foster entrepreneurial learning and support women entrepreneurs, resulting in an average score of 3.64 (see Figure 6.2). While Georgia and Moldova remain regional leaders on the topic, scoring above 4, Ukraine has made significant progress since 2020 as has Armenia, especially in the area of entrepreneurial learning. Azerbaijan has stayed constant in its approach to the two policy areas but shows a slight decrease in overall dimension scores due to the absence of policy documents, notably an action plan, for women's entrepreneurship. The country has, however, implemented ad hoc measures and programmes for female-led businesses, as further explained below.

## Figure 6.2. Entrepreneurial learning / women's entrepreneurship, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/6csogi

*Entrepreneurial learning*

## Table 6.2. Entrepreneurial learning, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **3.10** | **2.88** | **3.87** | **4.14** | **4.01** | **3.60** |
| Planning & design | 3.87 | 3.53 | 4.33 | 5.00 | 4.53 | 4.25 |
| Implementation | 2.90 | 2.73 | 3.64 | 3.91 | 4.05 | 3.45 |
| Monitoring & evaluation | 2.47 | 2.26 | 3.76 | 3.40 | 3.10 | 3.00 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

EaP countries continued to develop policy frameworks for entrepreneurial learning, addressing the topic in national policy documents. The latter, however, vary in nature: most countries include entrepreneurial learning in education strategies, sometimes for a specific level -- vocational education and training (VET) or higher education, for example – and Armenia and Georgia have additional provisions in their respective SME strategies. In Ukraine, entrepreneurial learning is embedded in the overarching economic strategy. These policy frameworks are most often associated with action plans, except in the case of Azerbaijan. However, not all countries have formal policy partnerships for entrepreneurial learning[1] in place.

While entrepreneurship as a key competence was already included in EaP national curricula at the time of the previous SBA assessment (albeit not always at all levels of education), this new round reveals further improvements across the region. Armenia, which had displayed modest performance in 2020 compared to its peers, has introduced changes in school curricula, notably emphasising the need to promote the development of an entrepreneurial mindset and related skills – as recommended in the SME Policy Index 2020. Azerbaijan also updated its curricula and launched new VET infrastructure and career guidance services, while Georgia has made further efforts to harmonise with EntreComp – although both countries' approaches to entrepreneurial learning remain rather focused on VET. Moreover, all EaP countries have worked towards introducing innovative learning and teaching methods. The COVID-19 pandemic has

prompted educational institutions, teachers and students to move to online learning solutions, resulting in the creation of dedicated platforms – such as Azerbaijan's "Free Learning Portal" (tehsilim.edu.az) and the All-Ukrainian Online School (osvitoria.org). Beyond these online portals, there are several examples of innovative tools that have been implemented i) in both lower and upper secondary schools (e.g. the Clasa Viitorului in Moldova and the "Social school entrepreneurship" project in Vinnytsia, Ukraine, which combines active learning and a flipped classroom) and ii) in VET education, e.g. in Georgia through the development of "Fablabs" (fabrication laboratories) in VET institutions.

Further progress has been made in teacher training, albeit to varying degrees across countries. Additional courses and materials have been developed in most countries, such as Armenia. Major progress has been achieved in Georgia through the newly established Skills Agency, which is notably active in creating teacher networks to foster peer learning, exchange of good practices, and collaborative teacher projects.

In addition, EaP countries have been working to develop non-formal learning, including on entrepreneurship. Since 2019, Azerbaijan, Moldova and Ukraine have introduced normative-legal frameworks to allow for the certification of competences acquired in informal ways, while almost all countries include related provisions in their policy documents on entrepreneurial learning. Moldova, for instance, has developed regional centres for entrepreneurial education in six cities across the country. Moreover, all countries continue to promote entrepreneurship among the general population through various tools such as information campaigns, role models and national award ceremonies – although no major change was recorded over the assessment period.

Co-operation between higher education institutions and businesses has intensified across the region, through different mechanisms and often with donor support – e.g. through Creative Spark partnerships in Armenia, or MoUs between KOBIA and universities in Azerbaijan. Collaboration between VET institutions and firms has also improved – through work-based learning in Moldova, for instance. These practices have been further implemented in non-business faculties since 2020, which is a welcome development, although they have been implemented only on an ad hoc basis and limited to VET and higher-education institutions. Co-operation between general schools and SMEs on entrepreneurial learning is still at a very early stage in the EaP region – yet such collaboration can be very useful to tackle skills mismatches.

Overall, while EaP countries show strong achievements in policy planning and design, more could be done to ensure effective implementation of entrepreneurship as a key competence, as well as monitoring and evaluation. Indeed, entrepreneurial competences are not always captured in learning outcomes, and not all learners engage in at least one practical experience. This round of the SBA assessment has revealed persistent challenges in terms of monitoring and evaluation, a thematic block that has been enriched with additional detail. While all EaP countries have some form of monitoring of entrepreneurial learning policies, only Georgia and Moldova produce publicly available reports annually. Students' progress in entrepreneurial learning is not systematically assessed, and students' labour market outcomes are tracked only on an ad hoc basis by some universities. Teacher competences with regard to entrepreneurship are also rarely evaluated, which results in limited insights on teachers' actual progress in that direction.

*Women's entrepreneurship*

### Table 6.3. Women's entrepreneurship, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **2.50** | **3.71** | **4.90** | **4.40** | **4.21** | **3.94** |
| Planning & design | 4.43 | 3.57 | 5.00 | 5.00 | 4.14 | 4.43 |
| Implementation | 1.53 | 3.80 | 5.00 | 4.20 | 4.33 | 3.77 |
| Monitoring & evaluation | 2.00 | 3.70 | 4.50 | 4.00 | 4.00 | 3.64 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Policy frameworks for women's entrepreneurship in EaP countries have not undergone major changes since the previous assessment. The new results reveal different trends across the region. Georgia and Moldova remain EaP leaders, with a steadily strong performance in all thematic blocks; Azerbaijan and Ukraine show a more unified picture across the sub-dimension than in 2020, when their scores were driven by a good performance in implementation; and Armenia's approach has been constant – the country has included women's entrepreneurship in policy documents but could still improve stakeholder co-ordination, awareness-raising, and monitoring and evaluation.

All EaP countries have implemented a range of women-specific business support services, albeit to varying degrees. In Moldova, the SME agency (ODIMM at the time, now ODA since 2022) re-conducted its programme *Women in Business* for three years in 2019, following a successful pilot version, and should soon approve a new follow-up *Women's Economic Empowerment Programme*. The comprehensive support provided by *Women in Business* (training, mentoring and co-financing) has helped aspiring women entrepreneurs gain managerial skills and increases their access to resources, services and technologies. While this full-fledged initiative remains unique in the region, gender-tailored accelerators have been developing in all five EaP countries (Table 6.4).

Additional measures have been implemented to address different barriers faced by women entrepreneurs. Armenia, for instance, has worked to ease their access to finance through preferential interest rates for aspiring entrepreneurs (introduced in 2020 by the Ministry of Economy, the Investment Support Centre fund and banks in response to the COVID-19 pandemic). In Ukraine, existing initiatives have been complemented by war-related support tailored to women, e.g. to help female entrepreneurs relocate and/or access business advisory, mentoring, psychological and other types of support (see Box 14.3 in the Ukraine country chapter). Most of these programmes across the region are promoted online, on the national web portals of SME agencies and/or business associations; however, Ukraine is the only country to have so far developed a one-stop shop providing an overview of existing support (Diia.Business, at business.diia.gov.ua)) – following a recommendation in the SME Policy Index 2020.

### Table 6.4. Selected examples of women-tailored accelerators in the EaP region

| Country | Programme | Year | Governance | Target group and coverage | Description |
|---|---|---|---|---|---|
| Armenia | Platform # 5 \| Upskilling | Launched in 2022 | Public and international organisation:<br><br>UNDP, Ministry of Labour and Social Affairs, Ministry of Economy | Disadvantaged women (unemployed, social benefits recipient, victim of domestic violence, caretaker of a disabled person, etc.)<br><br>Yerevan and regions | Free-of-charge courses, notably on digital marketing, for women outside the labour market.<br>Apart from video lessons and online tests, women can participate in group work activities and take advantage of career advice and mentorship. |
| Azerbaijan | Scale Up Accelerator | 2020 | Public-private: KOBIA, AQSIA, Ministry of Economy, State Committee on Family, Women and Children Affairs, US Embassy in Azerbaijan, PASHA Bank, PwC Azerbaijan | Women entrepreneurs in Azerbaijan | The eight-week programme provides courses on the topics of digital transformation, communication, investment rules, and self-development, with the goal of strengthening women's impact on the economy. |

| Country | Programme | Year | Governance | Target group and coverage | Description |
|---|---|---|---|---|---|
| Georgia | Empowering Women Entrepreneurs in Georgia | 2022 | Public, co-led with Estonia:<br>Estonian Ministry of Foreign Affairs<br>Estonian Refugee Council<br>Mtskheta-Mtianeti Regional Hub | Women living in the IDP settlements (Tserovani, Tsilkani, Prezeti, Shavshvebi and Khurvaleti) and in the administrative boundary line villages (Odzisi, Mchadijvari, Lamiskana and Kvemochala) | Five-day training event to develop entrepreneurial skills, followed by a six-month mentorship programme with experienced consultants for some of the business ideas developed, and a three-day business management training course.<br>The programme also offers financial support in the form of grants. |
| Moldova | Elevator Women Startup Accelerator | 2023 | NGO and international organisation:<br>NIKA Generation<br>Yep! Moldova<br>UN Women | Moldovan and Ukrainian startups based in Moldova with at least one woman on the team and with growth potential | Training and mentoring sessions in product development and market penetration, access to a network of startup founders. |
| Ukraine | Visionary Women's Accelerator "Vidvazhna" | 2023 | Public-private:<br>Ministry of Digital Transformation<br>Visa | Aspiring or current women entrepreneurs of micro and small businesses<br><br>Online and offline in ten Ukrainian cities | This programme gives a three-months course to women entrepreneurs, with topics ranging from customer relations to pricing and exports. At the end of the programme, the two best projects are given a financial reward. |

Source: (UNDP, 2022[10]); (Kobia, 2019[11]); (Estonian Refugee Council, 2022[12]); (Startup Moldova, 2023[13]); (Vidvazhna, 2023[14])

Moreover, support for women entrepreneurs has been expanding beyond capital cities. All countries have made significant progress in this regard by developing the territorial coverage of their national support programmes, and/or by implementing complementary measures and programmes directly in regions. In Azerbaijan, for instance, 17 women's resource centres have been created in different cities, notably providing training and consultancy services to help women launch their businesses (see Box 6.1), while Georgia has launched a pilot programme to support women's employment more broadly, aiming at integrating economically inactive women into the labour market and fostering their involvement in agriculture.

### Box 6.1. Azerbaijan's Women Resource Centres

In Azerbaijan, the State Committee for Family, Women and Children Affairs, in collaboration with the United Nations Development Programme (UNDP), has established Women's Resource Centres across different regions of Azerbaijan. These centres' core mission lies in empowering women, fostering their economic and social independence and active participation in socio-economic life, and promoting community development. To this end, the centres provide comprehensive support, including:

- ***Early-stage entrepreneurship***: Women can access assistance in developing business plans, receive consultations, and gain support in starting and running their own businesses. This also entails support in the registration process for new businesses, simplifying the procedure for starting new ventures.
- ***Vocational training***: The centres offer vocational training programmes to enhance women's skills and expertise in various fields, potentially improving their employability or business ventures.
- ***Financial literacy***: Women can receive training and guidance in financial management, budgeting and other financial skills to increase their financial independence and decision-making abilities.
- ***Gender equality education***: The centres provide education and awareness programmes to promote gender equality and advocate for women's rights.
- ***Non-financial support***: Women may receive material-technical assistance, including goods, equipment, furniture and accessories to support their business ventures or initiatives.
- ***Business monitoring***: Regular monitoring of business subjects is conducted to ensure progress and success, especially in areas such as agriculture, tailoring, baking and pottery.
- ***E-commerce***: Women are encouraged to improve their online selling opportunities for handmade products via training and guidance.

As of 2022, 17 Women's Resource Centres had been established in Azerbaijan, with over 13,000 women participating in different training sessions and events, and 617 having started a new business with the help of the centres.

Source: (UNDP Azerbaijan, 2023[15]), fact-finding exercises.

In addition, countries have pursued efforts to bridge gender gaps in STEM disciplines, including initiatives designed to increase girls and women's involvement in these fields. These efforts mostly focus on raising awareness, e.g. through annual events, and sometimes provide training in IT skills – in Georgia and Moldova, for instance.

Overall, support for women entrepreneurs has been strengthened by the active involvement of the private sector and international donors. On the one hand, business associations play a major role; for example, Azerbaijan's *Scale Up Accelerator for Women Entrepreneurs* is a public-private initiative co-implemented by the women's entrepreneurship development association AQSIA, while the Georgian Chamber of Commerce and Industry cooperated with UN Women on a project promoting gender equality and women's empowerment in the workplace. On the other hand, international organisations significantly contribute to – and at times drive – governmental efforts. An example is UNDP, which participates in the vast majority of existing programmes across Armenia (e.g. accelerators and small-grant projects with the SME Cooperation Association).

Despite these common trends, the assessment reveals substantial differences in policy frameworks for women's entrepreneurship across the region. Not all countries currently have a formal policy partnership on the topic, or an action plan with concrete measures, set targets and allocated budgets. Azerbaijan, despite its above-mentioned achievements in terms of support, currently does not have a strategic document or policy framework in place. Developing a more structured approach would help to ensure co-ordination between the different initiatives and actors (public and private, national and international) and to step up support for efforts to strengthen the capacity of non-governmental organisations (NGOs).

Women's entrepreneurial potential in the EaP region remains untapped. Relevant quantitative and qualitative data remain scarce, preventing regional comparisons, but the few insights available reveal persisting challenges. Women entrepreneurs still face more barriers than men – notably in terms of access to finance and networks. They tend to export less and are concentrated in lower-value-added sectors. In Ukraine, for instance, they mostly operate in retail sales (food beverages, tobacco, textile) and restaurants, mobile food service activities, and funeral businesses (Ukrstat, 2022[16]). Some 87% of women entrepreneurs operate only in their region, and only 7% export goods and/or services abroad (Diia.Business, 2023[17]). Moreover, data available for Georgia illustrates that women are under-represented in the sectors offering the highest wages (e.g. IT, professional, scientific and technical activities) – and, even in sectors where they outnumber men (e.g. accommodation, food services, human health, social work), they continue to be paid less than their male counterparts. Gender stereotypes and housework, enhanced by the COVID-19 pandemic and containment measures that increased the time spent on domestic tasks, further impede business development.

Understanding and tackling these remaining challenges requires, among other things, more and better data insights. EaP countries are not, for instance, included in international databases on the topic, such as the Global Entrepreneurship Monitor. Some studies are conducted to assess barriers to women's entrepreneurship in most EaP countries; however, apart from Ukraine, these are not conducted annually. Moreover, monitoring and evaluation of existing programmes could be improved in order to assess their concrete impact on women-led businesses and to identify persisting issues.

### *The way forward*

#### *Entrepreneurial learning*

Building on the aforementioned achievements and continued efforts to foster entrepreneurial learning at all stages of life, EaP countries could:

- **Strengthen policy frameworks for entrepreneurial learning** by introducing entrepreneurship as a key competence at all levels of education in Azerbaijan and Georgia and adopting formal national policy partnerships on entrepreneurial learning in Armenia.
- **Complement teacher-training efforts** by ensuring the inclusion of entrepreneurship in pre-service teacher training, and in in-service training at all education levels. Improvements could also be made in assessing the impact of teacher training, e.g. by regularly assessing teachers' competences in entrepreneurship.
- **Step up co-operation between secondary schools and SMEs, especially in general education.** Educational institutions and employers could exchange information and collaborate in a more systematic manner, thereby fostering student engagement in practical experiences. Surveys, such as those conducted by the Labour Market Information System of Georgia, suggest firms' demand for closer co-operation with the education system is still unmet.
- **Improve monitoring and evaluation practices in entrepreneurial learning**, ensuring the assessment of learning outcomes, and systematically track graduates' labour market outcomes to inform labour-market policy making.

*Women's entrepreneurship*

Moving forward, women's entrepreneurship policies could be further improved by:

- **Ensuring co-ordination among stakeholders** involved in women's entrepreneurship policies and programmes. Azerbaijan and Ukraine could adopt formal policy partnerships in this regard, clearly defining the role of each public and private sector actor and setting up co-ordination mechanisms among them, which would also help to ensure that efforts are complementary.
- **Improve data collection on gender-related issues and guarantee and improve impact evaluation for existing programmes**. Table 6.5 provides examples of indicators that EaP countries could consider collecting, in line with international standards. Regularly conducting studies on remaining barriers to women's entrepreneurship would also help in building a better understanding and fostering evidence-based policymaking.
- **Step up support by helping women entrepreneurs beyond the early stages of business development**. Most existing support programmes target early entrepreneurship, enabling women to launch their businesses. Moving forward, this approach could be complemented by measures to help women entrepreneurs scale-up their businesses. Enterprise Ireland's approach, notably its Competitive Start Fund for Female Entrepreneurs, offers an interesting example in that regard (see Box 6.2).
- **Address structural barriers** by further tackling remaining gender stereotypes and encouraging women to engage in higher-value-added sectors. The 2023 OECD Toolkit for Mainstreaming and Implementing Gender Equality offers useful guidance, including actionable measures and concrete examples, for policy makers working to promote gender equality at large (OECD, 2023[18]).
- **Develop incentives to reduce women's participation in the informal economy**. Only Georgia has taken measures in this direction so far, having conducted a study on the topic and developing a policy document based on the results. Azerbaijan and Ukraine have taken steps to reduce informality, but these do not yet entail women-specific provisions.

## Table 6.5. Examples of indicators for measuring women's entrepreneurship

| Institution/Organisation collecting/using the indicator | Indicators |
|---|---|
| OECD | Share of self-employed women who are employers<br>Share of self-employed women who are own-account workers<br>Share of self-employed in manufacturing<br>Share of self-employed in services<br>Share of women inventors |
| EU | Enterprises managed by the founder, by sex of the entrepreneur<br>Employees and self-employed persons by business function, NACE Rev.2 activity aggregate and size class<br>Employed persons being self-employed without employees by sex<br>Self-employment by sex, age, education |
| World Bank | Profits of microentrepreneurs by gender<br>Average profit for female entrepreneurs in male-dominated versus female-concentrated sectors<br>Characteristics of female entrepreneurs (e.g. age, marital status, household size, nr. of children, education) |
| Global Entrepreneurship Monitor | Female/Male total early-stage entrepreneurial activity<br>Female/Male opportunity-driven total early-stage entrepreneurial activity<br>Market focus (local, national, international) for early-stage entrepreneurs by gender<br>Household income by gender and region for early-stage entrepreneurs<br>Percentage of entrepreneurs with startup intentions, nascent activity, new business, established business, business exit by gender<br>Entrepreneurial perceptions by gender (e.g. fear of failure, startup skills, seeing new business opportunity, easy to start a business)<br>Industry distribution by gender of entrepreneur<br>Reasons for business exit by gender of entrepreneur |

Source: (OECD, n.d.[19]); (Eurostat, n.d.[20]); (World Bank, 2022[21]) (Global Entrepreneurship Monitor, n.d.[22]); (Global Entrepreneurship Monitor, 2022[23]).

### Box 6.2. Enterprise Ireland's support for women entrepreneurs

**Context**

The Action Plan for Women in Business – initiated by Enterprise Ireland, the Irish government's enterprise development agency – represents an ambitious and comprehensive strategy aimed at fostering greater representation of women in the business world, particularly in leadership positions throughout Ireland. Starting in 2020, this plan comprises four objectives:

- Enhance the presence of women-led established companies growing internationally.
- Augment the number of women in middle and senior management and leadership roles.
- Facilitate the rise of female entrepreneurs, encouraging more women to take the path of entrepreneurship.
- Boost the prevalence of women-led start-ups that exhibit high growth potential.

**Competitive Start Fund (CSF) for Female Entrepreneurs**

In line with these objectives, Ireland's Competitive Start Fund (CSF) for Female Entrepreneurs stands as the strategic scale-up funding initiative, backing women-led startups and businesses with both financial and non-financial support. Targeting specifically female entrepreneurs, the Fund aims at narrowing the gender gap in entrepreneurship and providing targeted support to women-led start-ups, promoting diversity and inclusion in the Irish start-up ecosystem.

The CSF focuses on start-ups with innovative and scalable business ideas with the potential for rapid growth and international market expansion. While the CSF primarily provides funding to early-stage start-ups, it plays a crucial role in laying the foundation for future scale-up success. Apart from product development, market validation, and pre-seed-stage and seed-stage support, Enterprise Ireland offers equity investment to eligible female entrepreneurs establishing new high potential start-up (HPSU) companies.

HPSUs are start-up businesses with the potential i) to develop an innovative product or service for sale on international markets and ii) to create 10 jobs and EUR 1 million in sales within three years of starting up. Enterprise Ireland's funding closely aligns with the company's stage of development, whether it is in the feasibility, investor-ready or growth stage. The selection process involves a competitive evaluation of the applicants' business plans, growth potential, market opportunities, and founding team capabilities.

Beyond funding, the selected entrepreneurs under the CSF can receive additional business support, such as mentorship, access to networks, and other resources to aid in business development and scaling. Mentorship plays a pivotal role in guiding entrepreneurs through the challenges of scaling their businesses and navigating the complexities of the market. CSF-recognised start-ups also gain visibility and validation within the entrepreneurial community, particularly among potential investors, partners, and collaborators, which is crucial for scale-up success.

By nurturing female-led start-ups at different stages of development, the CSF contributes to the overall growth and vibrancy of the start-up ecosystem in Ireland – creating jobs, driving innovation and contributing to the country's economic development.

Source: (Enterprise Ireland, 2020[24]); (Enterprise Ireland, 2022[25]).

## SME Skills

Skills shortages and mismatches are often quoted among the major challenges encountered by SMEs. They experience more difficulties than large firms in attracting and retaining skilled workers and providing their workers with upskilling and reskilling opportunities – which can in turn impede firm profitability and competitiveness. This is notably due to their lack of means, such as time and financial resources, to carry out and/or participate in training. SMEs also often lack awareness of their needs, of how training can help develop their business, and of the support mechanisms available – notably because of less-developed human resource management systems. They also face higher opportunity costs of training (OECD, 2021[26]).

Recent crises, such as the COVID-19 pandemic, along with the fast-paced development and spread of new technologies across economies and societies and the green transition, have been prompting changes in the nature of jobs and, consequently, in skills demand within labour markets. Recent data insights suggest that the skills required by the labour market changed by approximately 25% between 2015 and 2022, and that this number will likely double by 2027 (Roslansky, 2022[27]). Certain competences become redundant as a result of automation, while the demand for digital skills, for instance, is surging. According to the latest estimates, 1.1 billion jobs are likely to be radically transformed by technology in the next decade (World Economic Forum, 2023[28]). The Future of Jobs Report 2023 reveals that 43% of work tasks will be automated by 2027; six workers out of ten will require training by then, but only half of the workers currently seem to have access to adequate training options, and the most in demand are not always included in corporate upskilling strategies (World Economic Forum, 2023[29]). These trends create a pressing need for more investment in human capital. Creative and analytical thinking – as well as technological literacy, resilience, flexibility and agility – are among the most and increasingly sought-after competences among firms.

The importance of skills development among SMEs is reflected in EU documents, such as the *Next Generation SME Strategy*, and 2023 has been designated the European Year of Skills. Building stronger, diversified, and vibrant economies will require both SME managers and employees to gain the necessary enterprise skills to grow, create jobs, and further contribute to wealth creation. These competences will also allow firms to make effective use of their full potential and enhance competitiveness.

Equipping individuals with relevant skills and competences can be done through training opportunities and targeted financial and non-financial training incentives. It also requires multi-level, collaborative governance by public and private stakeholders, including government bodies responsible for economic, education and labour market policies; education and training providers; private and civil society organisations active in the fields; and firms themselves. Such co-operation also fosters comprehensive and systematic skills intelligence that then enables the design of policies, education and training provision that meets the skills needs of SMEs.

### *Assessment framework*

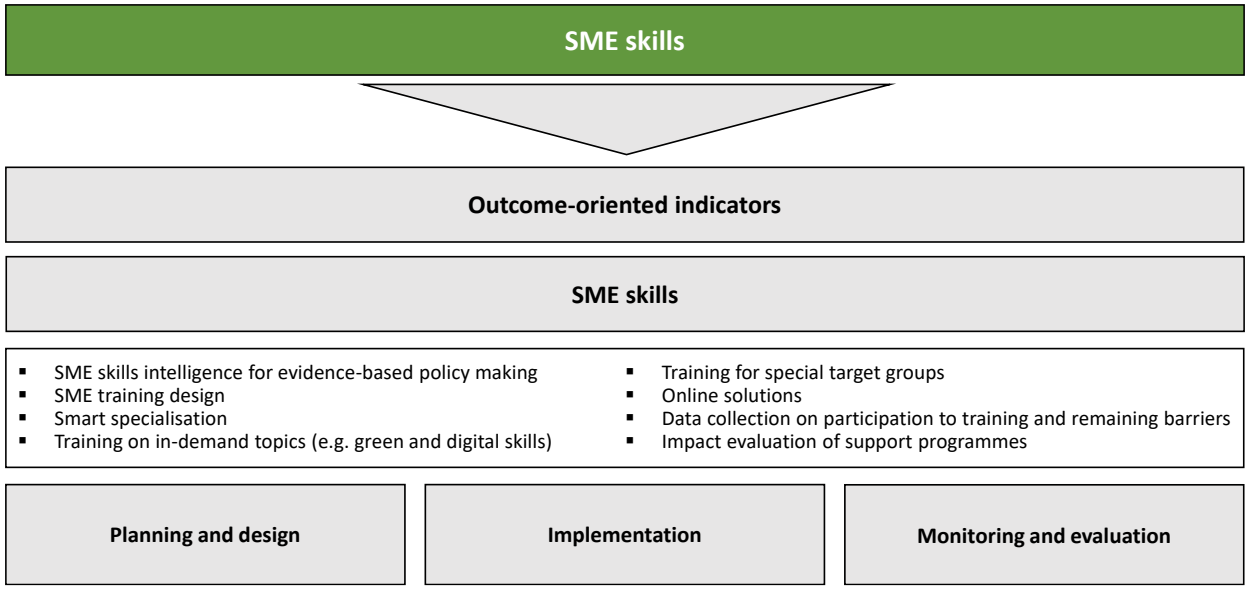
This dimension takes stock of the progress achieved by EaP countries in providing relevant training opportunities to SMEs, tackling obstacles to upskilling and reskilling among firms, and gathering skills intelligence to feed into policy making.

In comparison with the previous assessment, the framework now covers additional topics, corresponding to areas of increasing relevance (e.g. digitalisation, greening, intellectual property, social economy) and at times going more in-depth, e.g. on smart specialisation and on the availability of online courses. More emphasis is now placed on monitoring and evaluation, assessing skills intelligence on SME managers and employees, and more generally skills assessment and anticipation practices. Furthermore, the analysis considers countries' ability to regularly collect quantitative information to monitor the impact of policies on in-house and external training provisions for SMEs ("outcome-oriented indicators").

As a result, the assessment framework for this dimension comprises of the following:

- **SME skills** examines government policy for SME training in a range of areas and for various target groups (e.g. women and the youth). It assesses the existence of national frameworks for the collection and analysis of data on SME skills, available support for training, and monitoring and evaluation practices.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information about four indicators: i) the share of enterprises providing training to their employees; ii) participants in state-financed SME training, by sex; iii) the share of enterprises providing training to their personnel to develop/upgrade their ICT skills; and iv) the share of enterprises that employ ICT specialists, by enterprise size class.

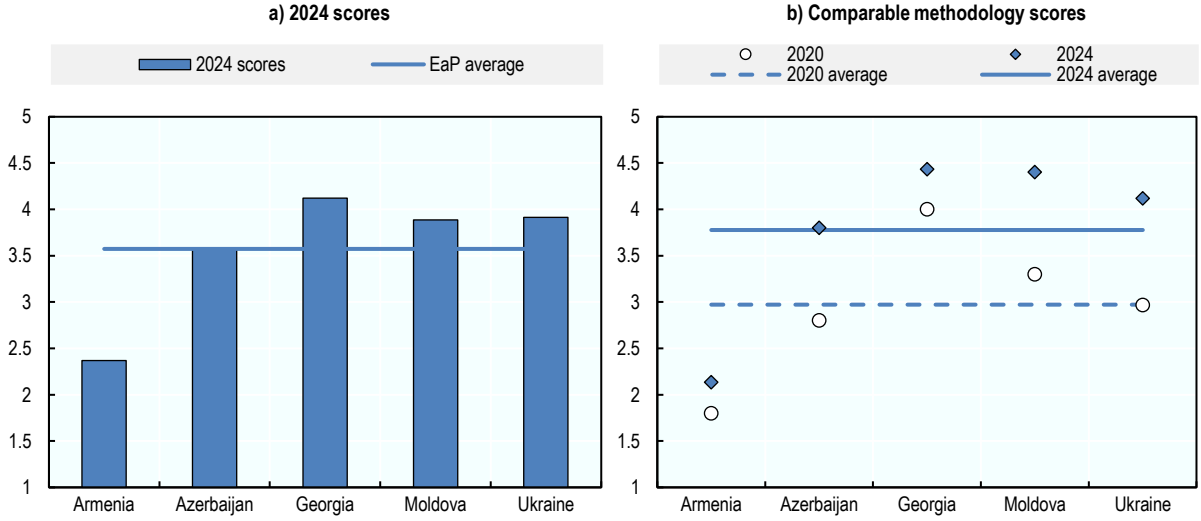
### Figure 6.3. Assessment framework – SME skills



## *Analysis*

*Regional trends and comparison with 2020 assessment scores*

### Figure 6.4. SME skills, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/g4zrot

All EaP countries have made progress in their approaches to SME skills development since the previous assessment, as reflected in a considerable increase in average scores, from 2.97 to 3.78 in the scores calculated based on a comparable methodology.

Moldova and Ukraine have been catching up with Georgia, which remains the EaP leader in the field. Azerbaijan is closely following, boosted by significant improvements in skills intelligence and training provision thanks to KOBIA's (the SME agency) efforts in that direction. Armenia has also made some progress, albeit more modest, having been notably slowed down by the restructuring of its SME support infrastructure.

However, the current lack of outcome-oriented indicators on skills and training slightly mitigates scores for all EaP countries, leaving considerable room for improvement.

*SME skills*

### Table 6.6. SME skills, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **2.41** | **3.76** | **4.25** | **4.10** | **4.01** | **3.71** |
| Planning & design | 1.67 | 3.13 | 4.49 | 4.69 | 3.39 | 3.47 |
| Implementation | 2.75 | 4.00 | 3.80 | 4.00 | 4.75 | 3.86 |
| Monitoring & evaluation | 2.67 | 4.11 | 5.00 | 3.44 | 3.11 | 3.67 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

This sub-dimension, the only one in this dimension, can be divided into two main themes: i) provision of training services for SMEs and ii) skills intelligence and its use for policy and practice.

Regarding training opportunities, the range of courses offered to SMEs has been expanded in the region. Azerbaijan and Ukraine have made particularly noteworthy progress in this regard. In Azerbaijan, KOBIA has created a network of operators (SME development centres, SME houses, SME Friends) across the national territory, with SME development centres conducting courses on a wide range of topics. In Ukraine, Diia.Business, launched in 2020 (see Box 14.4 in the Ukraine country chapter), now acts as an online 'one-stop shop' for entrepreneurial knowledge and consulting. Overall, EaP countries have worked to create new courses covering increasingly demanded skills such as digital and, to a lesser extent, green skills. Moldova is at the forefront in this regard, with ODA having implemented programmes in these two directions. Its SME digitalisation programme, launched in 2020 and re-conducted in 2022, remains, so far, the only full-fledged programme supporting the digitalisation of SMEs in non-IT sectors in the region, while Georgia has been actively working towards expanding its support in this direction. Armenia's current approach differs from that of its neighbours, with most of the SME/start-up skills development programmes being delivered by NGOs, most often with donor support; but the range of services available has also been widened, notably by the Enterprise Incubator Foundation and the increasing number of incubators and accelerators flourishing in the country.

Moreover, online training has become increasingly available in EaP countries, prompted by the COVID-19 pandemic and successive lockdowns. Its implementation is, however, advancing at different speeds in the region. Azerbaijan and Ukraine have dedicated online video training platforms on Kobim.az and Diia.Business, respectively; by contrast, although their EaP neighbours have moved some courses to a remote format (on an ad hoc basis) and launched new online training courses, these are not gathered on a one-stop-shop portal. Overall, these developments are very welcome and are helping to maximise training outreach beyond capital cities. However, the learning outcomes and overall impact of the materials launched so far could be further enhanced by making them more interactive. EaP countries, apart from Ukraine, have not yet introduced innovative digital learning methods such as gamification (i.e. game-like courses with learning objectives to be achieved) to improve SME skills.

With regard to smart specialisation, Georgia, Moldova and Ukraine have been further developing their approaches since the previous assessment. The three countries have worked on relevant policy documents: Ukraine addresses the topic in its *National Economy Strategy 2030* and *State Regional Development Strategy 2021-27*[2], with plans to implement regional development projects and SME support instruments; while Georgia and Moldova have prepared draft strategies, to be adopted soon. However, SMEs could be given more encouragement to tap into the potential of smart specialisation, e.g. through targeted training in identified priority areas. An analysis of skills implications could also be foreseen in the different areas to identify and address gaps. In terms of institutional frameworks, the three countries have worked to ensure co-ordination across stakeholders, through dedicated inter-ministerial groups most often involving a selection of public and private actors.

In parallel to training provision, most EaP countries have improved their frameworks for skills intelligence, and their use thereof. SME agencies in the EaP region, except in Armenia, collect sex-disaggregated statistics on training participants, as well as their feedback; this information then feeds into the development of new courses and/or adjustments to existing programmes. However, the concrete impact of training on skills development and SME performance is rarely assessed. Overall, national frameworks for the collection and analysis of data on SME skills have been strengthened in most countries. Georgia remains the regional leader in this regard, with its annual surveys of business demand for various skills, along with additional sector-specific studies. Starting from a weak basis in 2020, Azerbaijan has also made considerable improvements, and now collects insights on the training needs of entrepreneurs and in-house training within small firms – as recommended in 2020. Nevertheless, Armenia has not yet implemented such practices.

Finally, skills assessment and anticipation tools are still at a nascent stage in the EaP region. Apart from the above-mentioned surveys, they remain mostly limited to labour market analyses, with additional insights being provided by *ad hoc*, donor-led studies and other tools. The Edu2work platform launched in Armenia offers an interesting and innovative example in this regard, providing fresh insights on skills demand and inputs for national policies.

### *The way forward*

Moving forward, EaP countries could complement and strengthen their approaches to SME skills development by:

- **Raising awareness of available training offers**: Given the variety of public and private stakeholders involved in training provision for SMEs, gathering all opportunities in a single, one-stop-shop portal could help increase visibility and help SMEs navigate between the different options. Diia.Business offers a good example in this regard.
- **Further developing online training opportunities**: Building on the online courses that have been developed in recent years, EaP countries could consider introducing innovative and digital learning methods. Such practices can enhance learning outcomes through their interactive approach.
- Improving monitoring and evaluation practices by **capturing the impact of training on skills development and SME performance** – for example, through simple surveys conducted among participants after the training, asking about the extent to which skills have improved, and/or through skills assessment before and after the course, to allow for objective evaluation. Training providers could also consider following up with trainees a few months after the programme.
- **Considering introducing certification of the skills acquired**, which would help ensure the quality of training and flag competences to hiring managers.
- **Introducing/strengthening systemic approaches to data collection** on SME skills, including for the green and digital transitions, training needs analysis, as well as barriers to participation in training. Countries could step up efforts in this regard, collecting more granular insights on a regular basis, and developing a database of indicators on SME skills to inform policy making.
- **Implementing skills anticipation tools**, such as sectoral studies and quantitative forecasting models (see Box 6.3).
- **Strengthening smart specialisation approaches by developing targeted support** for innovative, competitive, and growth-oriented SMEs **in the priority areas**. Vocational education and training provision could be updated in these priority areas.

### Box 6.3. Skills assessment and anticipation tools

**Overview**

Skills assessment and anticipation exercises are usually defined as activities designed to estimate future skills needs in the labour market "in a strategic way, using consistent and systematic methods". They can be highly valuable tools that allow policy makers to capture the changes in skills demand and supply and to develop relevant measures to prevent and/or address skills shortages and mismatches.

They can take a variety of forms, ranging from simple surveys (among employers and/or school/training graduates) to quantitative projections based on macroeconomic modelling. Examples include:

- Skills surveys
- Quantitative forecasting models / projections
- Qualitative methods involving experts
- Sectoral studies
- Foresights and scenario development
- Graduate tracer studies

A combination of different methods, both quantitative and qualitative, can help to build a keen understanding of current and upcoming trends.

**Example: OSKA Estonia**

OSKA is the Estonian anticipation and monitoring system for labour and skills demand, analysing the labour and skills necessary for Estonia's economic development over the next 10 years. It has been conducting sectoral studies of labour and skills needs since 2016, anticipating skills needs over the next 7-10 years in every sector of the Estonian economy (up to five sectors per year).

It combines qualitative and quantitative methods, using statistical data from various surveys (e.g. on labour force, education, Population and Housing Census, sectoral surveys) and qualitative personal interviews and group discussions (e.g. sector experts, policy makers, education providers). This enables policy makers to draw conclusions, identify mismatches and formulate suggestions.

Conclusions are derived from sectoral expert panels composed of one-half employers, one-quarter educational institutions, and one-quarter policy makers. They oversee the process, validate the results, and help ensure dissemination and follow-up.

OSKA has become a well-known and acknowledged system that is widely used by target groups. Its strengths lie in its multi-stakeholder approach, the fact that a similar methodology is applied to all sectors, and the follow-up done on results and recommendations. The intelligence collected is used in policy making. Recent examples of resulting adjustments include planning and adjusting VET and university curricula; developing a government project to promote growth occupations; and planning migration measures and digital re-training and up-skilling projects.

Source: (ILO, 2015[30]; OECD, 2016[31]; OSKA, 2022[32]).

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## Notes

[1] A *formal partnership* defines a relationship between a number of organisations (public, private, civic) with agreed objectives to support entrepreneurial learning policy and its implementation. The partnership has resources (human, financial or other) to support the administration and development of the partnership and its activities, as well as a clearly identified lead institution, mandate and calendar of activities. A structured national partnership (as opposed to an informal partnership) for entrepreneurial learning comprises appointed members from the state bodies (e.g. Ministry of Education, Ministry of Economy, Ministry of Labour), national agencies (e.g. SME agency), employers' organisations, trade unions and NGOs (e.g. youth entrepreneurship associations). Its objectives are a) to ensure co-operation between the range of players in the entrepreneurial learning eco-system, b) to ensure synergy and efficiency across the range of entrepreneurial learning activities in the country (as defined within national policies for lifelong entrepreneurial learning) and c) to provide advice to the government on developments in life-long entrepreneurial learning. The partnership's lead institution could be the Ministry of Education and could involve rotating leadership amongst its members. The roles and responsibilities of each member are clearly defined through an official document. The national partnership has a budget to support its work (e.g. engage expertise, organise roundtables, publicity).

[2] Moreover, all regions have been requested to conduct a mid-term review and adjustment of their regional development strategies, including the smart specialisation chapters, until 2027.

# 7 Pillar C – Access to Finance

One of the key challenges to SMEs' growth and competitiveness remains access to financial resources. This chapter elaborates on the latter and is structured around six components: 1) the legal and regulatory framework for bank financing, which addresses the protection of creditor rights, the use of a register and a credit information bureau, banking and stock market regulations; 2) bank financing, which essentially covers credit guarantee schemes; 3) non-bank financing, which looks into the use of microfinance, leasing and factoring; 4) the venture capital ecosystem, which analyses the enabling framework and the presence of business angel networks; 5) financial literacy, i.e. governmental efforts to disseminate financial know-how to businesses and citizens; and 6) digital financial services and the relevant regulatory and supervisory frameworks. Policy recommendations on how to further facilitate access to finance for SMEs are formulated at the end of this chapter.

## Introduction

Access to finance is a crucial pillar of SME growth and development. Being able to access external finance can allow a company to invest in new assets that will support its growth, develop new products and processes, and manage its finances more efficiently to enable it to become more competitive. As a result, access to finance can accelerate economic growth in an economy.

However, access to finance remains a challenge for SMEs across the globe, including in the Eastern Partner (EaP) region. A pre-COVID assessment of the global SME finance gap estimates that 41% of formal MSMEs in developing countries have unmet financing needs (SME Finance Forum, 2023[1]). In the EaP region, the financing gap is estimated to be around USD 44 billion (EUR ~41 billion, the equivalent of an average of 18% of the countries' GDP), meaning that for SMEs' needs to be fully served, current lending would need to increase by 200%. Given the COVID pandemic, war and economic challenges, these figures have likely not improved.

Obtaining credit can be challenging for many SMEs. Being small and having a wide range of differing needs, SMEs tend to be more difficult to reach and serve than larger companies. They carry a higher perceived risk of default, and their loans are more costly to manage given the fixed costs involved in providing a loan of any size. In many countries, especially those where financial sectors are not particularly deep, banks rely heavily on collateral, preferably immovable assets such as land or buildings. However, many small businesses lack sufficient immovable assets to use as security for loans. In addition, many small business owners possess only limited financial literacy, meaning that identifying the right financial product, preparing adequate accounts and presenting a convincing business case for a new investment can be challenging.

While some of these challenges are related to SMEs' inherent characteristics, many stem from deficient framework conditions and can be addressed or alleviated through government action. A robust legal framework for secured transactions can reduce the lender's risk, an adequate regulatory framework can ensure the sustainable development of the financial sector, and a legal framework supportive of the development of non-bank financing instruments can broaden the options SMEs have available for external finance. In addition, government policies such as credit guarantees can help borrowers with little collateral access funding, and programmes to boost investment in early-stage companies can help start-ups develop and grow. Measures to improve financial literacy can help entrepreneurs make better financial choices and submit loan applications with a higher prospect of approval. Finally, the development of digital financial services can help address some of the issues around scale when it comes to SME access to finance, thus opening up new and more affordable funding opportunities that are more tailored to the needs of small businesses.

Creating the right conditions for the development of a financial sector capable of responding to SMEs' needs is therefore fundamental – a necessity that the Small Business Act for Europe recognises. This chapter analyses different aspects of access to finance and the policies that support it and looks at both the supply and demand sides when it comes to credit provision.

### Table 7.1. Pillar C, country scores by sub-dimension (2024)

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2020 (CM)* |
|---|---|---|---|---|---|---|---|---|
| **Access to finance** | **3.54** | **3.31** | **4.07** | **3.48** | **3.40** | **3.56** | ***3.90*** | ***3.67*** |
| Legal and regulatory framework | 4.03 | 4.13 | 4.31 | 4.33 | 3.70 | 4.10 | *4.32* | *4.29* |
| Bank financing | 2.30 | 2.34 | 3.74 | 2.67 | 2.54 | 2.72 | *2.93* | *2.33* |
| Non-bank financing | 4.56 | 3.61 | 3.71 | 4.04 | 4.22 | 4.03 | *3.98* | *3.60* |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2020 (CM)* |
|---|---|---|---|---|---|---|---|---|
| Venture capital | 3.34 | 2.04 | 3.56 | 2.32 | 2.52 | 2.75 | *2.65* | *2.00* |
| Financial literacy | 4.53 | 3.27 | 4.80 | 2.94 | 3.94 | 3.90 | *3.80* | *3.38* |
| Digital financial services | 3.52 | 3.05 | 3.94 | 3.02 | 3.81 | 3.47 | - | - |
| Outcome-oriented indicators | 3.00 | 3.22 | 4.56 | 2.78 | 3.22 | 3.36 | - | - |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Access to finance

### *Assessment framework*

This pillar covers six dimensions relevant to access to finance: i) the legal and regulatory framework for bank financing; ii) the provision of bank financing; iii) the conditions for non-bank financing; iv) the ecosystem for venture capital; v) financial literacy; and vi) digital financial services.

Some important methodological changes have been implemented for this pillar since the last assessment. Most prominently, a new dimension on digital financial services has been added. Given the importance of digital finance for SME credit and the new avenues it opens up to provide more affordable and accessible funding to small businesses, it seemed necessary to expand the assessment framework under this pillar. In addition, outcome indicators have been grouped into one scoring dimension rather than being distributed across thematic sub-dimensions. This change intends to put emphasis on the availability of data points and highlight the importance of data collection as a basis for informed policy decisions.

There have also been some smaller changes to the remaining dimensions, but these are mostly focused on clarifying certain questions to improve the ability to answer and score them. Some new questions have been added. For instance, the inclusion of environmental, social and governance (ESG) aspects in the banking regulatory framework is now being considered given the rising importance of such matters for the finance world, as well as the impact climate change may have on banks' portfolios. In the non-bank financing sub-dimension, new questions around the regulation of microfinance have been introduced where previously only availability and supervisory aspects were covered. Governments were also asked to provide information about policies put in place during the COVID pandemic to support SMEs' access to funding when sales dried up due to lockdowns (Box 7.1).

### Box 7.1. Government measures to support SME access to finance during the COVID-19 pandemic

During the pandemic, governments across the EaP region introduced measures with a view to stabilising their economies. Among these were measures that focused on providing funding to ensure business continuity and facilitating the management of payment defaults by commercial banks. These included support programmes as well as regulatory adjustments. The aim was to keep businesses afloat, to maintain employment, and to avoid a rapid rise in non-performing loans in the banking sector.

While there is variation across countries in terms of specific measures, some commonalities exist. The majority of measures were introduced in the first quarter of 2020 (and updated thereafter), and most were phased out in the course of 2021, with only a few exceptions. The most commonly used measures include the following:

- **Interest rate subsidies**: several governments introduced interest rate subsidies in order to help keep businesses alive. Some of these loans benefitted from interest-free periods (e.g. Armenia) or reduced rates (e.g. Georgia, Ukraine), and eligible loan purposes were defined relatively widely so that loans could be used for salaries, utility payments, rent, working capital and even refinancing of existing debt (e.g. in Ukraine).
- **Grants**: One-off payments, especially to small and micro businesses, were also quite common, for example in Armenia, Azerbaijan and Ukraine. Some grants also targeted specific sectors such as tourism or agriculture.
- **Credit guarantee schemes**: In all EaP countries, credit guarantees were either introduced or expanded in order to help businesses cope with the strain from lockdown measures. Typically, measures included the increase in the guaranteed amount (to 80-90% for individual exposures), reduction in guarantee fee payments (to 0% in certain cases), and expansion of eligible loans (in terms of minimum or maximum amounts or eligible use of proceeds).
- **Payment deferrals and management of loan portfolios**: Central banks in all EaP countries encouraged commercial banks to apply more flexibility in terms of repayment schedules for borrowers that were struggling. In some countries (e.g. Azerbaijan, Moldova and Ukraine) these were also accompanied by changes in macroprudential measures, such as capital and liquidity requirements or loan classification and provisioning obligations, i.e. being able to maintain a certain loan classification even in case of repayment holidays. The National Bank of Georgia introduced a liquidity support instrument to support SME lending by allowing banks to use their SME loan portfolios as collateral. Under the programme, it was also possible to defer principal and interest payments for SME clients, and 50% of SME borrowers benefitted from this measure.

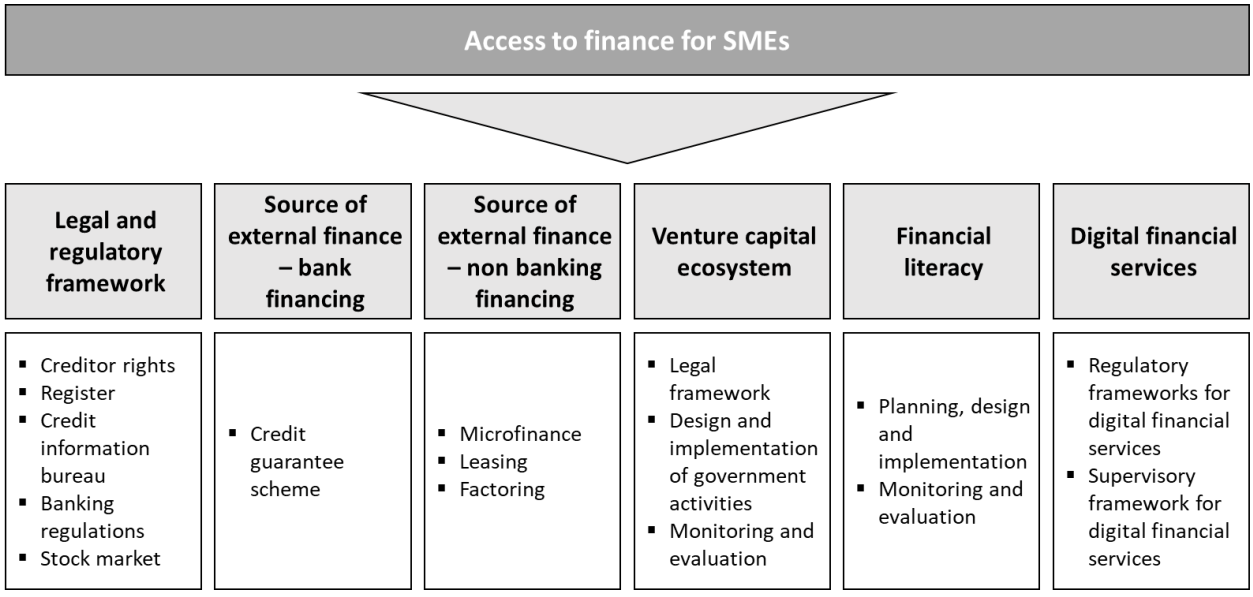
Although credit levels in some cases are still below crisis levels, these measures supported the continued functioning of both the banking sector as well as the real sector, laying the foundations for positive credit growth going forward.

Source: (IMF, 2021[2]); EaP government accounts.

Overall, access to finance is the result of a complex interaction of different determinants, including the macroeconomic environment, monetary policy, the health and breadth of local financial markets, and the creditworthiness of enterprises. The assessment framework cannot capture all these factors, but instead focuses on a set of topics which are deemed disproportionately important for SME access to finance:

- **Legal and regulatory framework**: this sub-dimension focuses on the legislation facilitating access to finance, including protecting creditor rights, facilitating the use of collateral and credit information, and banking and stock market regulations.
- **Bank financing**: this sub-dimension covers bank lending practices and the availability of credit guarantees.
- **Non-bank financing**: this sub-dimension reviews the legal framework and use of microfinance, leasing and factoring.
- **Venture capital**: this sub-dimension assesses the legal framework enabling venture capital (VC) and the existence of business angel networks.
- **Financial literacy**: this fourth sub-dimension analyses government efforts to promote financial know-how among the business community and wider population.
- **Digital financial services**: the last sub-dimension covers the existence of a regulatory and supervisory framework for a range of digital financial services.
- The section on **outcome indicators** considers countries' ability to regularly collect statistical information about the following indicators: outstanding business loans (SMEs and total); new business lending (SMEs and total); short-term loans (SMEs, initial maturity < 1 year); long-term loans (SMEs, initial maturity > 1 year); government loan guarantees (SMEs); government guaranteed loans (SMEs); interest rates for new business loans (SMEs and large firms); collateral requirements (SMEs); VC investments; leasing and hire purchases; factoring and invoice discounting; microfinance loans; non-performing loans (SMEs and total); and payment delays (business-to-business).

### Figure 7.1. Assessment framework – Access to finance




## *Analysis*

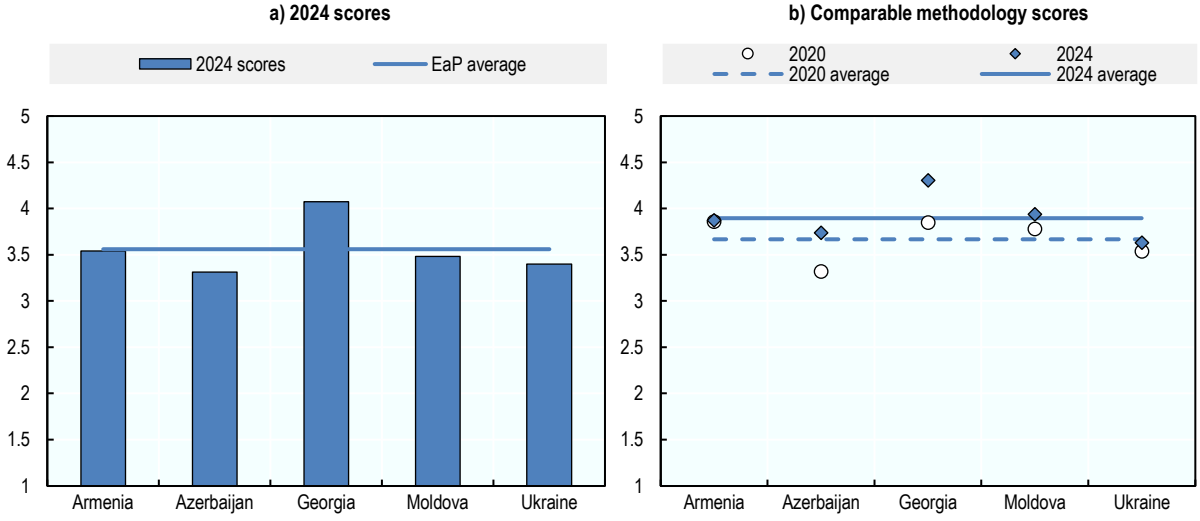
*Regional trend and comparison with 2020 assessment scores*

Due to the methodological changes and new dimensions that have been introduced, the 2020 and 2024 scores are not directly comparable; however, much of the movement and variation across countries and

sub-dimensions can be noted and certain trends can be discerned. For instance, policies across almost all sub-dimensions have improved, with many governments putting in place new or larger support schemes for access to finance, introducing legal reforms to improve the framework conditions for non-bank financing solutions and conducting more regular financial literacy assessments. Another aspect that has led to improvements in the scores for this sub-dimension is the removal and grouping of outcome indicators that used to suppress scores. As is common in the policy world, changes on paper do not necessarily translate into immediate improvements in outcomes for a variety of reasons: time lags in legal or policy changes feeding through to actual outcomes, deteriorations in the macro environment that counterbalance positive policy changes, and other influencing factors.

On the other hand, methodological changes that led to the addition of more ambitious objectives, such as the consideration of ESG aspects in the regulatory framework, meant that scores were lower than if these additional elements had not been introduced. This affected scores in the opposite direction, leading to an overall score that suggests very little has changed when in fact quite a lot has happened in this pillar, as will be explained in more detail in the following sections.

## Figure 7.2. Access to finance, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### *Legal and regulatory framework*

Having an adequate legal and regulatory framework for SME access to finance is a fundamental prerequisite for bank lending to SMEs, especially since small firms are typically seen as riskier borrowers. Therefore, much of the legal framework for secured transactions focuses on reducing lending risk. For instance, having registers in place allowing security interests to be established facilitates the use of collateral, which means that the bank has a chance of recovering at least part of its money if the borrower defaults. However, such registers need to be accompanied by fair and efficient enforcement processes so that lenders can get quick access to the collateral if enforcement is necessary. Similarly, credit information systems can help reduce information asymmetries and therefore decrease the perceived riskiness of a borrower.

Having adequate prudential measures in place is important to ensure that the banking sector remains healthy and able to lend, and provisions to encourage local currency lending are useful from both a financial

stability and consumer protection perspective, as unhedged borrowers may be at a higher risk of default if taking out a foreign currency loan when exchange rate movements are a realistic possibility.

### Table 7.2. Legal and regulatory framework, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **4.03** | **4.13** | **4.31** | **4.33** | **3.70** | **4.10** |
| Creditor rights | 3.20 | 4.10 | 4.10 | 5.00 | 3.20 | 3.92 |
| Register | 4.86 | 4.91 | 5.00 | 4.81 | 4.90 | 4.90 |
| Credit information bureau | 4.32 | 4.32 | 4.32 | 4.32 | 4.32 | 4.32 |
| Banking regulations | 3.40 | 2.90 | 4.09 | 3.00 | 1.26 | 2.93 |
| Capital market | 4.16 | 3.71 | 3.71 | 3.71 | 3.89 | 3.84 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

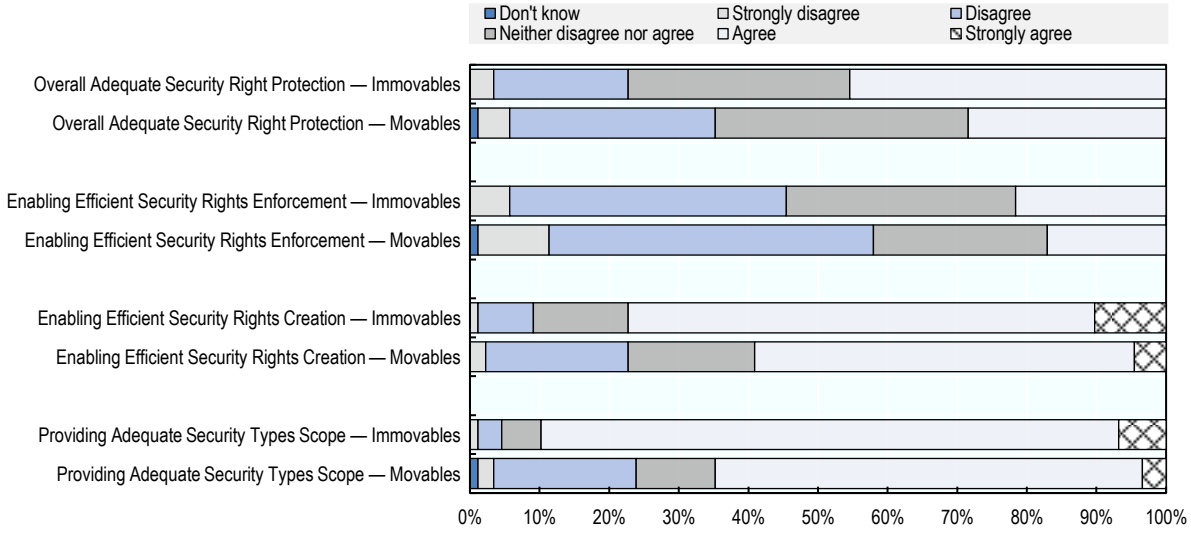
#### Creditor rights: Legal frameworks for secured transactions are in place but enforcement remains an issue across the region

All economies in the region have a reasonably developed legal framework for secured transactions in place and scores have only changed marginally in this sub-dimension. Enforcement continues to be of concern, however. This issue has been consistently flagged throughout the assessments, but progress to address it has been slow. If enforcement is inadequate, this impacts the entire framework, as creditors will not be able to make use of collateral and take steps to recover their funds if a borrower defaults, even if the process of defining and registering an asset as security was straightforward.

A survey of banks across the region shows that they are generally satisfied with the scope of the types of security that can be used, as well as with the process of creating security rights. There is some difference between types of assets, with immovable assets being assessed as more favourable. However, 46% of respondent banks disagree or strongly disagree with the statement that "the existing framework enables the efficient enforcement of security rights over immovable assets", and this share increases to 57% for movable assets. This points to widespread dissatisfaction when it comes to enforcement mechanisms thus compromising the willingness of lenders to provide credit to smaller firms.

Further information related to this topic can be found in the Pillar A chapter under "Bankruptcy and second chance".

## Figure 7.3. Bank responses: assessment of the law and its implementation related to immovable and movable assets, EaP total




Source: (EBRD, 2020[3]).

StatLink https://stat.link/ekd9pw

### Register: Collateral registers are available in all countries but accessibility could be improved in some cases

Having reliable and accessible registers that facilitate the use of immovable and movable assets as collateral is important for a legal framework for secured transactions. Up-to-date information and accessibility are crucial to ensure that lenders can check whether a certain asset is already pledged and register their own security interest.

There have not been any major changes to how the existing registers are operating since the last assessment. Cadastres exist in all countries and are available online and to all stakeholders. In Azerbaijan, access used to be restricted but has been broadened to the general public. Registers for movable assets are also in place across the region and all financial institutions can access them. They are fully available online in Armenia, Azerbaijan and Georgia, but only partially available online in Moldova and Ukraine. In Ukraine, online access was restricted after Russia's invasion and access has to be specifically requested.

When it comes to practical application, a recent banking survey suggests that cash-flow analysis, knowledge of the client, personal collateral and immovable assets are the most important factors that lending decisions are based on. Guarantees (by governments and individuals), automated credit scoring, and movable collateral seem to play less of a role in bank's lending decisions (EBRD, 2020[3]).

### Credit information

Credit information systems can be useful in reducing information asymmetries between lenders and borrowers and facilitating the creditworthiness assessment of an SME asking for finance. There are generally two types of credit information system: 1) a public register, usually run by the central bank or financial authority; and 2) a private credit bureau, a company that collects credit information and makes it available to financial service providers for their credit assessments. Public credit registers tend to only take information into account that the central bank collects from the banks and other financial institutions it supervises. A private credit bureau can collect information from a wider range of sources, such as financial service providers that do not fall under the supervisory authority of the central bank, utilities,

telecommunications companies, insurance companies and others. This usually allows them to build a fuller picture of a potential borrower, especially if that borrower lacks a history of borrowing and repaying.

In some markets, credit information providers are increasingly trying to use digital technologies to assess the risk of a borrower's default based on a wider range of data, such as behavioural and social information. These types of credit scoring mechanisms are particularly relevant in the context of digital financial services (see under "Digital financial services" later in this chapter) but can also supplement more traditional credit scoring.

All central banks in the region have a credit register, and each country has at least one (if not more) private credit bureau, with a private credit agency opening up in Azerbaijan for the first time since the last assessment. Borrowers in all EaP countries have a legal right to access their credit information. In terms of coverage, most credit bureaus go beyond collecting information from financial institutions, but sources of credit information could be further expanded in some countries, such as Moldova and Ukraine. Since the discontinuation of the World Bank's Doing Business data collection, new comparable data on population coverage of credit information are not available, but data up to 2020 suggest that credit coverage was less than 60% of the population in Azerbaijan, Moldova and Ukraine, whereas it was relatively high (above 80%) in Armenia and Georgia.

### Banking regulations

A robust supervisory framework is important for maintaining a healthy banking sector capable of extending credit to companies and households. Many of the measures that are examined in the context of this assessment are about reducing risks within the system. For instance, the adoption of Basel III principles puts in place prudential measures that ensure banks manage portfolio risks well and have sufficient buffers to withstand more difficult times. Regulation to encourage local currency lending aims to reduce defaults due to exchange rate shifts and also has an element of consumer protection. In all of the Eastern Partner economies, foreign currency loans tend to be cheaper than local currency loans, making them an attractive, albeit higher-risk, option for unhedged borrowers. Ensuring that banks recognise and manage this risk, and that clients are aware of the potential ramifications of taking out a foreign currency loan, is particularly important in this type of environment.

Countries have made progress with the implementation of Basel III requirements. Where only Georgia had fully implemented them in the last assessment, Moldova has now followed suit, and Armenia, Azerbaijan and Ukraine have made progress on implementation. Ukraine, in particular, relaxed some prudential requirements after the full-scale invasion and, consequently, Basel III implementation is delayed. Expectations are, however, that they will progress in 2024 if the situation allows.

Loan dollarisation levels have decreased since the last assessment, with between 55% and 80% of loan portfolios now denominated in local currency. Except in Ukraine, all central banks have put in place certain requirements to encourage local currency lending, such as higher risk weights and mandatory disclosure of foreign exchange risk to borrowers.

Finally, it is increasingly important to take ESG (environment, social & governance) considerations into account in regulatory frameworks. Climate change can have a significant impact on banks' portfolios. For example, extreme weather events can damage companies' and households' assets, or impact the revenue generation of agricultural companies, which in turn can affect a borrower's repayment capacity.

The inclusion of ESG-related indicators in banks' reporting obligations is not yet widespread, however. Georgia is the only country where banks need to systematically report on these aspects, and the National Bank of Georgia is the only financial authority in the region that has already developed a green taxonomy to facilitate the correct classification of green financing instruments. The central bank is also working on introducing climate-related stress testing. In all other countries, these developments are still at an early stage. In some instances, governance-related issues are being monitored, albeit at the bank level rather

than the borrower level. Environmental or social aspects do not form part of any disclosure requirements, however. There is still a long way to go for these considerations to become a firm part of the central bank's supervisory framework, but work has begun and should lead to further improvement in the next assessment.

### Capital markets

The notion of financing SMEs through capital market instruments has gained traction in recent years. If tailored to SME needs, capital markets can provide a viable alternative financing option for companies at the higher end of the SME size spectrum. Companies can use capital markets to access more long-term financing, in the form of either an initial public offering (IPO) or corporate bonds. In both developed and emerging markets, attempts have been made to make capital market instruments more accessible for SMEs, albeit with mixed results. One common constraint involves the fixed costs associated with capital market instruments, which make smaller amounts of financing less worthwhile. But fundamentally, ESG - oriented instruments need to be developed and liquid enough to provide a viable financing option for corporates in the first place before moving on to SMEs.

None of the markets in the region are sufficiently developed to be seen as a realistic funding option. Although each country has a stock exchange, they tend to be characterised by issuances of government or bank bonds with a limited investor base. Market capitalisation as a percentage of GDP is low, with an illiquid secondary market. In some instances, restrictions on institutional investors restrict the investor pool, which contributes to limited liquidity.

#### *Bank financing*

In all markets, both developed and emerging, bank financing is the most important source of external finance for SMEs. Many factors influence accessibility and affordability: the enabling environment for bank financing (as discussed in the first part of this chapter), the macroeconomic environment, competition in the financial sector and many more. Governments can work on the enabling environment to support the development of a healthy private banking sector that can serve borrowers who are able to take informed financial decisions. They can also run support schemes that target SMEs' access to finance specifically, addressing some of the market failures that SME lending suffers from.

These schemes can take different forms, such as interest-rate subsidies, grants or credit guarantees. While the government's choice of instrument can depend on various factors, it is important that any scheme be designed with several considerations in mind: how it addresses the identified policy issue, what sunset clauses are being introduced to avoid over-dependence, how the support scheme can be designed to minimise the risk of market distortion, and what evaluation mechanisms are put in place to monitor their effectiveness and adjust if necessary. The last point is particularly crucial to ensure that whatever option is chosen addresses the identified policy issue and supports the intended outcomes, therefore minimising the potential waste of public funds.

**Table 7.3. Bank financing, sub-dimension scores**

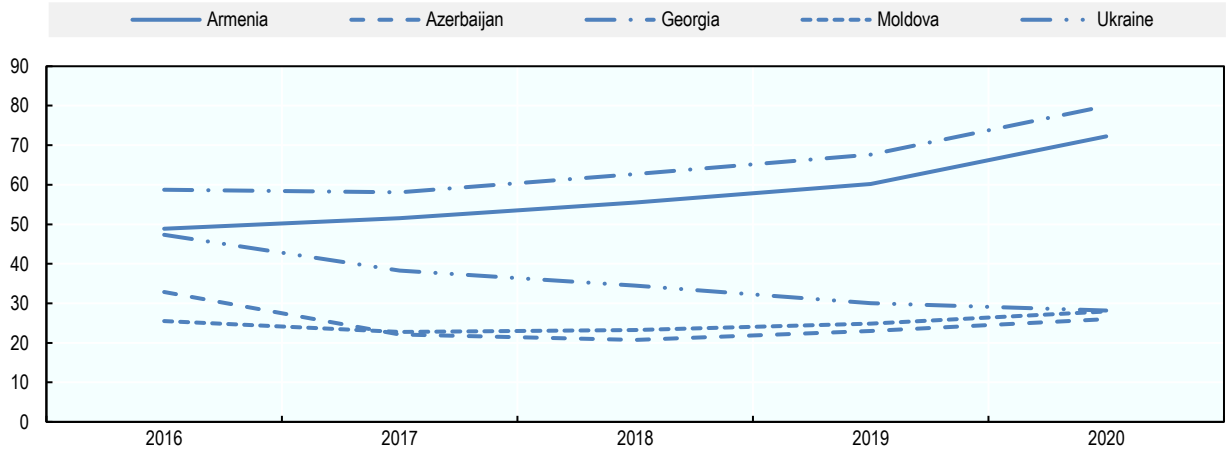
| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **2.30** | **2.34** | **3.74** | **2.67** | **2.54** | **2.72** |
| Banking lending practices and conditions | 2.66 | 2.32 | 3.31 | 2.66 | 2.50 | 2.69 |
| Credit guarantee schemes | 1.78 | 2.38 | 4.38 | 2.70 | 2.61 | 2.77 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### Banking lending practices and conditions

A number of countries in the region have recently experienced major upheavals in their banking environments, that have impacted lending conditions in the years since. Azerbaijan, Moldova and Ukraine all experienced difficult periods in the banking sector that required major clean-up and recovery measures by their respective central banks. These activities have helped stabilise sectors, but in the meantime lending has remained subdued (see Figure 7.4) and the COVID pandemic has further delayed recovery. Overall, the ration of domestic credit to GDP ranges from as low as 26% in Azerbaijan to nearly 80% in Georgia. Levels are higher than during the last assessment, but still well below the OECD average (102%).

## Figure 7.4. Domestic credit to the private sector as a percentage of GDP (2016-20)

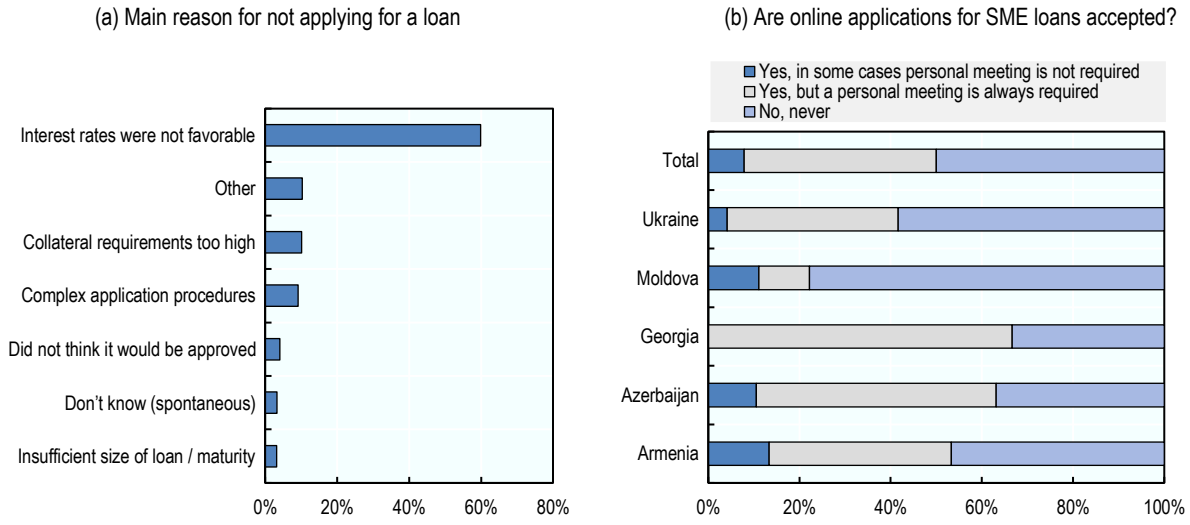



Source: (World Bank[4]).

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According to some estimates, there is a funding gap equivalent to 18% of GDP across the EaP region, and around a third of SMEs are reportedly credit constrained, meaning they would like a loan but cannot access one (SME Finance Forum, 2023[1]). According to a business survey conducted in 2019, the reasons for not being able to access a loan when needed were mainly linked to high interest rates, but high collateral requirements and complicated application procedures also played an important role (EBRD and World Bank, 2020[5]). While interest rates and collateral requirements are the result of a complex set of factors, easing barriers to loan applications is something that can be remedied more easily. However, when looking at the ease of submitting a loan application, a recent survey of banks shows that online applications that do not require a physical presence are not common and in half of the cases, no online application is possible at all (Figure 7.5) (EBRD, 2020[3]). This chapter also discusses elements that can address the issues of high interest rates (e.g. a robust secured transactions framework for digital financial services) and high collateral requirements (e.g. credit guarantees, which are explored in the following section).

## Figure 7.5. Barriers to SME bank finance in EaP countries




Source: (EBRD and World Bank, 2020[5]).

### Credit guarantee schemes

Credit guarantees can be an effective instrument to support SME access to finance. They can help de-risk loans, especially where collateral is lacking. They also tend to be more aligned with commercial lending practices than, for example, interest rate subsidies. Lending decisions are still based on an assessment of risk, and an interest rate is set to reflect that risk. Credit guarantees also tend to be more cost-effective than subsidies. Money has to be paid only in case of a default, whereas subsidies are a continuous expense that cannot be recovered. Therefore, if well-managed, credit guarantee schemes can be less onerous on public budgets.

All economies in the EaP region have credit guarantee schemes in place. Armenia, however, is currently going through a restructuring, which means that the design and future of its scheme is currently uncertain. Azerbaijan and Georgia put in place credit guarantees during COVID specifically to help businesses in particularly challenging times; those schemes are still in place. Moldova expanded its programme nearly tenfold between 2020 and 2022. Increasingly, these guarantee programmes are supplemented by an offering of consultancy and advisory services to help entrepreneurs with their business development. All schemes still rely on government budget transfer, however, rather than being fee-based, and are therefore more self-sustainable. In addition, it would be good to strengthen private participation in the schemes, especially in Armenia and Azerbaijan. This can be done by inviting business associations or private banks to participate in some form of advisory or even supervisory capacity and even consider commercial banks' participation on the scheme's capital. Except in Georgia, none of the schemes are subject to proper impact evaluations that ascertain whether policy objectives, such as increased access to finance or expanded financial inclusion, are being achieved. All of them are subject to some reporting on basic metrics such as volumes disbursed and the number and characteristics of borrowers.

### *Non-bank financing*

Non-bank financing instruments can play several roles in improving access to finance for SMEs. They can offer financial services that are more tailored to SMEs' needs and circumstances, and they can promote financial inclusion by offering products to borrowers that are not able to access bank funding due to their size, lack of credit history or lack of collateral.

This dimension covers microfinance, leasing and factoring as three of the most prominent non-bank financing instruments that are relevant for SMEs. While microfinance is available at a large scale across the region, leasing and factoring levels are still quite low compared to other economies of a similar size. The reason for the low uptake can be inadequate legal frameworks that introduce legal uncertainty to providers and users of a certain product. Another frequent reason is a lack of awareness, as entrepreneurs do not have knowledge of these financing options or how they could be beneficial. Finally, data on these sectors can be patchy or non-existent, making assessments of their health and prospects rather difficult.

### Table 7.4. Non-bank financing, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **4.56** | **3.61** | **3.71** | **4.04** | **4.22** | **4.03** |
| Microfinance institutions | 4.40 | 4.08 | 5.00 | 4.64 | 4.60 | 4.54 |
| Leasing | 4.71 | 3.51 | 5.00 | 4.71 | 5.00 | 4.59 |
| Factoring | 4.70 | 3.35 | 1.25 | 2.90 | 3.20 | 3.08 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### Microfinance institutions

Microfinance is available throughout the region, through banks, credit unions or specialised microfinance institutions (MFIs). Data are not available for all countries, but statistics from Azerbaijan and Georgia show that microfinance has either increased or been stable since the last assessment, meaning that even during COVID there has not been a significant shrinkage of the sector. This is particularly noteworthy for Azerbaijan, where between 2015 and 2017 the number of customers of MFIs halved due to the more general challenges in the banking sector. In Armenia, microfinance loans have dropped by 30% since 2019 (Central Bank of Armenia, 2023[6]). However, this might be due to the sector consolidating after the introduction of a legal framework for microfinance activities. Ukraine still does not have a dedicated legal framework for microfinance in place.

Across the region, microfinance continues to target mainly households and, consequently, an increasing number of governments are putting in place consumer protection measures to avoid customers from being charged excessive interest rates. One example is Moldova, where the financial regulator sets limits on how much MFIs can charge consumers. Microfinance providers tend to be self-sustainable throughout the region, but most are not allowed to raise deposits, which can hamper the sector's development, as entrepreneurs cannot bank with MFIs as a one-stop shop for all of their financial needs.

#### Leasing and factoring

Leasing and factoring are asset-based financing tools that can provide access to credit for enterprises without sufficient collateral or where information asymmetries are particularly high because funding is directly tied to an asset of equal value. Leasing can allow businesses to acquire equipment or vehicles necessary for their operations, modernisation or growth without having to provide additional collateral. Factoring means that a business sells its accounts receivable from a client with good credit standing in order to receive liquidity before payment of the invoice is due. In one permutation of this instrument, reverse factoring, a large buyer of goods and services is involved in setting up a factoring facility that allows select suppliers to get working capital from a bank or specialised finance provider against its invoices. This enables SME suppliers to have access to working capital priced against the credit risk of the larger buyer rather than their own.

Leasing and factoring are available in all economies in the EaP region. In a number of countries, such as Georgia, they are provided through commercial banks. Azerbaijan and Georgia have completed the

reforms of their legal framework for these instruments since the last assessment. In Ukraine, however, the reform of the factoring framework has not begun, although it could help alleviate existing uncertainty around this instrument and boost uptake.

### *Venture capital*

Venture capital is nascent in the entire region and the lack of growth capital beyond the seed stage presents a real challenge for start-ups. Most countries have start-up grants and accelerator programmes in place to help with the initial stages of development, but once a business enters the growth phase it is important to attract private investors and not just rely on state funding. While the presence of venture capitalists (individuals or funds) is largely determined by the availability and attractiveness of investment targets, governments can contribute to the development of a venture capital ecosystem. Having a conducive legal framework for equity investments, such as robust minority shareholder protection, is an important prerequisite – which is present in all five countries. Governments can also introduce policies that incentivise VC activities, e.g. through co-financing schemes, investments in VC funds or the establishment of a fund of funds that provides capital to VC funds potentially interested in the country or region. The Armenian government, for example, invested in the country's first venture capital fund in 2013. The fund has gone on to make a number of investments in tech-focused start-ups in the country and has made its first successful exits since. Activities like this can be a good use of public funding to catalyse the sector and leverage public funds for private investment.

**Table 7.5. Venture capital, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.34** | **2.04** | **3.56** | **2.32** | **2.52** | **2.75** |
| Legal framework | 3.78 | 3.44 | 4.11 | 3.44 | 3.44 | 3.64 |
| Design and implementation of government activities | 3.75 | 1.40 | 3.67 | 2.04 | 2.47 | 2.66 |
| Monitoring and evaluation | 1.67 | 1.00 | 2.33 | 1.00 | 1.00 | 1.40 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### *Financial literacy*

All the other dimensions in this pillar look at supply-side issues, but to promote access to finance for SMEs, it is also important to look at obstacles on the demand side. Increasing awareness of the range of financial instruments helps firms evaluate their options and find the best funding solution for their needs rather than always reverting to bank loans as the sole source of external finance. Ensuring that entrepreneurs are capable of preparing accurate accounts is an important factor in reducing information asymmetries for lenders, thus decreasing risk, and consequently the cost of a loan. Greater financial literacy among the population also means that entrepreneurs are more capable of interacting with financial service providers and take informed decisions, especially at the more vulnerable micro end of the spectrum. It is also important to have financial literacy assessments and trainings specifically designed to target entrepreneurs, in addition to the general population. Entrepreneurs have different needs than households when it comes to preparing loan applications and choosing financing instruments, as requirements tend to be more complex and the range of instruments broader.

However, the first step toward building greater financial literacy among the population is an assessment of financial skills within the population (including entrepreneurs). The assessment should cover different aspects of financial literacy, as in the OECD's framework for assessing financial literacy[1]. This helps to disaggregate knowledge, attitudes and behaviours and design policy measures that target the weakest

areas. All countries in the region conduct financial literacy assessments, usually led by the financial regulator, and in some cases supported by international donors (e.g. Ukraine).

Trainings and awareness-raising campaigns are important policy tools to improve the population's financial literacy. Armenia and Ukraine also stand out by having introduced centralised platforms that bring together training materials and knowledge products aimed at a range of audiences, such as pupils, teachers, the general public and businesses. Such platforms can be immensely helpful, as they provide impartial information and advice; are easily accessible; and, through their modularity, their offering can be adjusted if needed. Incorporating financial literacy into school curricula can be another effective way to raise the population's understanding of financial concepts. Financial literacy is mandatory for general and vocation tracks in Armenia and Ukraine; in the other countries, it is either optional or mandatory only for some schools.

### Table 7.6. Financial literacy, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **4.53** | **3.27** | **4.80** | **2.94** | **3.94** | **3.90** |
| Planning, design and implementation | 4.75 | 3.50 | 4.75 | 3.10 | 3.94 | 4.01 |
| Monitoring and evaluation | 3.67 | 2.33 | 5.00 | 2.33 | 3.93 | 3.45 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *Digital financial services*

Digital financial services have developed quite rapidly in recent years. They can enhance existing financing structures, but can also be a way to leapfrog toward greater financial inclusion and better SME access to finance in the face of underdeveloped financial markets. They can also help address some of the common issues around SME finance. Digitising processes can help scale solutions and make decision and management processes around loan provision more efficient. This can help banks scale their SME lending and bring down costs. New sources of data such as data from non-bank sources for credit analysis can provide a more reliable assessment of the borrower's repayment capacity and therefore reduce information asymmetries. A number of fintech-based products can help address a lack of collateral by using asset-based lending techniques, using movable assets or relying on better credit assessment, therefore reducing the need for collateral. In addition, new products are being developed that are better tailored to SMEs' needs, such as mobile digital payment devices.

Digital financial services are typically delivered by new players, such as specialised fintechs, big tech companies or mobile network operators, and challenger banks – although, increasingly, traditional banks are offering them as well. These services often focus on a single product or a limited range of products. The new players coming to the market with their customer-focused solutions can induce competition, which can lead to better or cheaper financing products and a greater desire by finance providers to serve more hard-to-reach segments. Indeed, when fintechs first started to appear on the financing landscape, many banks viewed them as competitors. This has changed, however. Increasingly, banks – and fintechs – realise that they can form mutually beneficial relationships, fintechs becoming service provider not just to consumers, but also to banks. These links can improve banking service provision by introducing new products or processes that make banking easier or cheaper. However, in markets that are not yet very developed, or that have an imbalance in terms of market dominance, the use of digital tools by one bank can lead to more concentration. If other banks in the market are unable to follow suit, an early adopting bank can cement its leading market position. While in and of itself not an issue, regulators need to be vigilant to detect any abuse of market power that could ensue.

Overall, however, digital financial services can open up new avenues to develop financial markets and reach SME clients whose financing needs have not been met by traditional banking models. Therefore, the developments over recent years provide a huge opportunity to improve SME access to finance, and hence the inclusion of this new dimension in the assessment. This dimension covers two main aspects:

- **The regulatory framework** – the institutional set-up for addressing issues related to digital financial services; the relevant authority's regulatory approach; and how operational risks are being managed, including data protection and the outsourcing of certain banking functions.
- **The supervisory framework** – the use of regulatory tools that are aligned with the rapid technological developments in the sector, e.g. the use of "regulatory sandboxes", or supervisory technology ("suptech").

## Table 7.7. Digital financial services, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.52** | **3.05** | **3.94** | **3.02** | **3.81** | **3.47** |
| Regulatory frameworks for digital financial services | 3.74 | 3.60 | 4.37 | 3.55 | 4.11 | 3.87 |
| Supervisory framework for digital financial services | 3.30 | 2.50 | 3.50 | 2.50 | 3.50 | 3.06 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### Regulatory frameworks for digital financial services

The emergence of digital financial services poses legal and regulatory challenges. In many emerging jurisdictions, the roll-out of digital financial services can be limited by existing legal and regulatory frameworks that need updating for new solutions to work, or their full benefits to be realised. Therefore, adjustments to the regulatory framework are often needed to account for new risks associated with these technologies, but also to allow new solutions to develop and take hold in the market (some of this will be discussed in the next section).

Foundational conditions are also important: the availability of reliable Internet services, digital identities, e-signatures and e-invoicing are all tools that support the development of digital financial services. But new technologies also pose their own risks, such as the emergence of new monopolies, more entrenched financial exclusion, as well as data protection and privacy concerns. For example, the use of new sources of data for credit scoring purposes can help households and SMEs access funding that was underserved by the traditional banking system. At the same time, many of these solutions use algorithms that can be somewhat of a black box when it comes to credit decisions, and that can perpetuate certain discriminatory practices as they learn from existing decision-making processes. Given the interdisciplinary nature of the challenges that digital financial services pose, it is crucial to have a more collaborative approach to regulation, ensuring that different public authorities are involved in developing policies that affect this sector.

Regulators also need to ensure interoperability of systems and certain standards for data collection and sharing so that new players can access valuable data in order to develop their new funding solutions. And greater access to finance also requires greater financial literacy among the population so that consumers and businesses understand what these new solutions mean for them, especially in an environment where regulation sometimes has to play catch-up.

Regulatory frameworks in the region are only at the beginning of their adjustment to these new challenges. While all financial authorities have a department with a dedicated mandate to cover digital financial services, only Ukraine has a dedicated digital finance strategy in place. In Georgia, aspects of digital

finance are covered in the central bank's strategy. In Azerbaijan, a digital payments strategy has been developed, thus covering one important area within the digital finance space.

All countries have regulation in place around data protection and sharing, and all authorities, except for Armenia, require institutions to share data under certain rules and circumstances, according to specific standards. All financial authorities have adopted a technology-neutral approach to digital financial service regulation, and do not have specific provisions for big tech solutions in place. An operational resilience framework for financial service providers is also in place in all of the countries, but only Armenia, Georgia and Moldova have a framework to regulate the outsourcing in the financial service sector, e.g. when a bank contracts a third-party provider to implement certain processes.

#### Supervisory framework for digital financial services

The emergence of new financial services and associated entities means that regulators need to balance differing objectives that can at times compete with one another: financial innovation, consumer protection and financial stability. In addition, the supervisory framework needs to ensure that new solutions that would bring benefits to the market can actually develop and are not immediately stifled by existing regulation that may or may not be relevant to addressing the risks associated with this specific type of new product or service.

In response, regulators have developed new regulatory tools. One of the more prominent tools is the regulatory "sandbox", a ringfenced space in which new financial products or services can be tested with consumers. The key here is that the scale is small (pilot), that consumers who use the product can easily raise the flag in case of a problem and that the regulator has a very close eye on how things develop. Some regulators also require the financial company to (partially) compensate consumers who test this new product in case things go wrong. Georgia is the only country in the region that has developed such a sandbox approach, which has already been used, mainly by banks, to test new methods of service provision such as digital banking. Setting up regulatory sandboxes requires significant investment in resources, however. Therefore, regulators should consider setting up innovation offices if other instruments are not yet realisable for the time being. An innovation office provides a focal point within the regulator for digital financial service providers to get clarity over regulatory requirements and to inform the regulator of their plans. Such a set-up can be an important tool for two-way communication between digital finance providers and the regulator and can be helpful in determining what the existing regulatory framework means for digital financial services and whether it may need adapting.

Given the complexity of some of the issues these new products and services raise, as well as the novel nature, multi-disciplinary co-operation between authorities is crucial to ensure that all potential risks are covered. Digital finance raises issues related to data protection, consumer protection, competition, ICT regulation, and many more. Ensuring that all of these aspects are taken into account is important to having a functioning and conducive supervisory environment. Currently, none of the countries in the region have a systematically implemented multi-disciplinary approach to digital finance supervision, even though some ad hoc consultations may be conducted. Learning from others is also important across borders. Networks of supervisory authorities focusing on digital finance can be an excellent avenue to learn from international experience and get a glimpse into where the sector might be headed. However, none of the financial authorities are part of such a network.

### *The way forward*

As highlighted above, SME access to finance could be further improved in the EaP region, and governments can help address the identified issues by focusing on the following actions:

- **Improve enforcement frameworks for secured transactions.** Enforcement is a crucial element of a functioning secured transaction legal framework. Without being able to make use of the

collateral that has been taken, loan costs will be unnecessarily high to account for the risk or cost involved in the enforcement process. In this context, out-of-court mechanisms should also be considered, especially for smaller loan amounts typically associated with SME lending. Because these mechanisms can be less costly in terms of both time and money, they can benefit both the lender and borrower.

- **Ensure adequate monitoring and evaluation mechanisms for financial support programmes.** All countries in the region have some form of support programme in place to facilitate SME access to finance. In the case of subsidies, these can be quite costly, and evaluations are paramount to determine whether greater financial inclusion has actually been achieved. The monitoring and evaluation framework therefore needs to go beyond the collection of basic usage data, such as number of clients reached or volumes of funds disbursed. In addition, it should involve an analysis of the types of borrowers who benefitted, whether they would have been able to access funding in the absence of the programme, and the programme's economic impact.
- **Improve the availability and collection of statistics in the financial sector**. While data on bank lending are usually available, they could be expanded to obtain more information on the type of borrower. Usually, disaggregation by size is possible, but not necessarily by other metrics, such as gender, type or location. However, such granular statistics are important to identify issues with sub-groups that may require targeted policy intervention. Data collection for non-bank financing sources should also be improved to be better able to pinpoint whether and why certain instruments are not taking hold.
- **Consider the establishment of support mechanisms for developing growth-stage funding for start-ups**. Successful policies to help the sector develop mainly rely on co-financing options, with a focus on catalysing private investment. Examples are government participation in specific VC funds, or the establishment of a fund of funds.
- **Facilitate access to knowledge and learning resources for financial literacy**. Online platforms can be a powerful tool for making information about existing public support and trainings available to different segments of the population. To maximise impact, it is important to tailor these trainings to different target groups: students, business owners, households, etc. The benefit of online platforms is that they are widely accessible; are modular, meaning that they can be adjusted as necessary; and provide neutral financial advice to individuals and business owners. A good example in this regard is the Single Access Point for SMEs (biznis.gov.me) in Montenegro, launched in 2022. The platform brings together useful information for entrepreneurs around access to finance, posts updates on relevant legal and regulatory changes, presents available support programmes and provides an interface for submitting questions to the Ministry of Economy. There are also good examples within the EaP region, including the Diia.Business platform in Ukraine and the abcfinance.com and fininfo.am websites in Armenia.
- **Develop strategic directions for digital financial service regulation and supervision and adopt a multi-disciplinary approach**. A strategy document, whether stand-alone or part of the financial authority's strategy, is important for identifying key challenges, establishing strategic direction and pledging necessary resources. Digital financial services are an emerging field that is complex and fast moving. It is therefore crucial to equip regulators with the human capital and tools necessary to address looming challenges. Part of this process is a new, more open approach to regulation in which both public and private stakeholders are regularly consulted.

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## Notes

[1] For more information, see https://www.oecd.org/daf/fin/financial-education/core-competencies-frameworks-for-financial-literacy.htm

# 8 Pillar D – Access to Markets

Pillar D examines the progress made by Eastern Partner countries regarding SMEs' access to both domestic and foreign markets. The chapter starts by looking at policies and tools in place to allow SMEs better access to public procurement markets, focusing on the legal frameworks and the strategies developed to support SME participation. It then reviews recent improvements in standards and technical regulation, looking at overall co-ordination and general measures, level of harmonisation with EU *acquis*, SME access to standardisation, and digitalisation of standards and technical regulations. Finally, this chapter investigates efforts to boost SME internationalisation through support for export promotion, SME integration into GVCs, and the use of e-commerce, as well as through the adoption of trade facilitation measures. For each one of these three areas, a set of dedicated policy recommendations is provided to guide EaP countries in their strategic actions for the forthcoming years.

## Introduction

Both domestic and international markets represent major opportunities for SMEs in the Eastern Partner (EaP) region. However, due to limited capacity and resources, they often struggle to tap into these markets.

Easier access to public procurement can provide SMEs with significant business opportunities in domestic markets and offers notable growth potential (European Commission, 2021[1]). SMEs' involvement in public procurement can also bring advantages to the public sector, as it can result in greater competition – leading to better value for money, efficiencies for contracting authorities (ADB, 2012[2]) and the development of innovative solutions.

Similarly, increasing globalisation and growing international trade offer SMEs the opportunity to join global value chains (GVCs) and to specialise within production networks, contributing to innovation and productivity growth (OECD, 2023[3]). Finally, the use of e-commerce allows firms to dramatically increase customer and supplier bases and reach markets beyond traditional physical boundaries (OECD, 2021[4]).

Nevertheless, small businesses face significant challenges in tapping into these markets. These include a lack of information about export opportunities, internationally incompatible quality standards, discriminatory rules and complex application procedures for public tenders. Finally, financial and human capital constraints hinder SMEs' access to international markets and public procurement.

Against this background, a proactive attitude to global competition and markets is increasingly a matter of necessity. Policy responses are needed to ensure that SMEs turn the pressure of international competition into an opportunity to increase quality and competitiveness, and thus to participate in the growth of international and domestic markets.

Targeted polices and support programmes can help to mitigate these impediments and further open market opportunities for SMEs. This pillar investigates recent reforms in the EaP countries in these areas by assessing three policy dimensions: 1) public procurement; 2) standards and technical regulations; and 3) SME internationalisation. Table 8.1 presents the 2024 scores for the EaP countries.

Before delving further into the analysis of this pillar, however, it is worth mentioning that there are important interlinkages between the various pillars and dimensions of the SME Policy Index: the public procurement sector can prosper only in an environment of reduced informality and corruption. Therefore, a strong institutional framework and level playing-field conditions are key elements for a healthy public procurement system and access to markets as a whole. Moreover, internationalisation of SMEs contributes to an increase in productivity, quality and innovation by exposing SMEs to international competition and helping them achieve economies of scale. Finally, access to, and uptake of, business development services (BDS) are also fundamental to promoting internationalisation. Advanced BDS and enterprise skills can provide firms with the knowledge and resources they need to internationalise by offering them targeted information, training, mentoring and consulting.

### Table 8.1. Pillar D, country scores by dimension and sub-dimension (2024)

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2020 (CM)* |
|---|---|---|---|---|---|---|---|---|
| **Public procurement** | **2.80** | **2.55** | **3.61** | **3.16** | **3.61** | **3.15** | ***3.13*** | ***3.59*** |
| Public procurement | 3.00 | 2.72 | 3.68 | 3.40 | 3.58 | 3.28 | - | - |
| Outcome-oriented indicators | 1.00 | 1.00 | 3.00 | 1.00 | 3.86 | 1.97 | - | - |
| **Standards and regulations** | **3.60** | **3.20** | **4.37** | **4.13** | **3.86** | **3.83** | ***3.98*** | ***3.67*** |
| Overall co-ordination and general measures | 5.00 | 3.23 | 5.00 | 4.33 | 5.00 | 4.51 | *4.51* | *4.51* |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2020 (CM)* |
|---|---|---|---|---|---|---|---|---|
| Harmonisation with EU acquis | 3.58 | 3.30 | 4.42 | 3.94 | 4.40 | 3.93 | *3.93* | *3.89* |
| SME access to standardisation | 3.85 | 3.25 | 4.13 | 4.55 | 2.83 | 3.72 | *3.82* | *3.00* |
| Digitalisation of standards and regulations | 1.50 | 2.13 | 3.63 | 2.50 | 2.50 | 2.45 | - | - |
| Outcome-oriented indicators | 3.67 | 3.67 | 5.00 | 5.00 | 5.00 | 4.47 | - | - |
| **SME internationalisation** | **2.91** | **3.25** | **4.52** | **3.45** | **3.77** | **3.58** | ***3.62*** | ***3.11*** |
| Export promotion | 3.57 | 3.67 | 4.84 | 4.28 | 4.30 | 4.13 | *4.11* | *4.12* |
| Integration into global value chains | 1.23 | 2.16 | 4.80 | 2.77 | 3.76 | 2.94 | *3.03* | *1.92* |
| OECD Trade Facilitation Indicators | 3.88 | 3.60 | 4.22 | 3.22 | 3.15 | 3.62 | *3.62* | *3.26* |
| Use of e-commerce | 2.25 | 3.44 | 4.00 | 3.31 | 2.89 | 3.18 | *2.99* | *1.72* |
| Outcome-oriented indicators | 4.00 | 3.00 | 4.00 | 2.00 | 4.00 | 3.40 | - | - |

Note: CM = comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Public procurement

Worldwide, the share of public procurement in overall public expenditure is often large, creating an important market opportunity for SMEs. By number, SMEs make up the bulk of the enterprises as well as of the suppliers of the public sector. However, they typically have a lower share of the total value of public procurement, partly because their participation rate is lower than that of larger enterprises.

At the same time, SMEs are often particularly innovative and may offer solutions that larger companies cannot provide. Increasing the generally low participation rate of SMEs in public procurement could therefore spark greater competition, generating better value for money for public purchasers and counterbalancing dominant market players (SIGMA/OECD, 2016[5]). However, this requires continued reform efforts to improve policy making, the regulatory and institutional environment, and the public procurement practices, complemented by raising the level of professionalisation and improving electronic procurement. In this context, ensuring access for potential competitors of all sizes and business characteristics constitutes a key requirement for a well-functioning public procurement system. This point is highlighted by the OECD Recommendation of the Council on Public Procurement under the principle of access (Box 8.1).

### Box 8.1. OECD Recommendation of the Council on Public Procurement – Principle on Access

The *OECD Recommendation of the Council on Public Procurement* (2015) contains the OECD's overarching guiding principles for promoting the strategic and holistic use of public procurement. It is a reference for modernising procurement systems and can be applied across all levels of government and state-owned enterprises. It addresses the entire procurement cycle while integrating public procurement with other elements of strategic governance such as budgeting, financial management and additional forms of service delivery.

Among other principles, the Recommendation states that OECD Members and non-Members adhering to the Recommendation ("Adherents") should facilitate access to procurement opportunities for potential competitors of all sizes. To this end, Adherents should implement coherent and stable institutional, legal and regulatory frameworks. Key features of the Recommendation include:

- **Characteristics of public procurement frameworks.** The framework should be clear and simple. Requirements should not duplicate or conflict with other legislation or regulation. The frameworks should treat bidders, including foreign suppliers, in a fair, transparent and equitable manner, giving consideration to Adherents' international commitments.
- **Tender documentation.** The extent and complexity of information required in tender documentation and the time allotted for suppliers to respond should be proportionate to the size and complexity of the procurement. Tender documentation should be standardised where possible, to ensure that tender opportunities are designed to encourage broad participation, including from new entrants and SMEs.
- **Use of competitive tendering.** Competitive procedures should be the standard method for conducting procurement as a means of driving efficiencies, fighting corruption, obtaining fair and reasonable pricing and ensuring competitive outcomes.

Source: (OECD, 2015[6])

Some SMEs shy away from tendering because they perceive the rules and procedures as complex and lengthy, and they often lack the human and financial resources and know-how to deal with the administrative requirements. These requirements are usually the same for all companies; when they are burdensome, they expose SMEs to relatively greater financial risks through potentially fruitless participation. Clear, simple procedures supported by a well-functioning e-procurement system would go a long way towards addressing this issue.

Among other issues limiting SMEs' participation in public procurement is the size of public contracts. In many cases, very large contracts are not justified, and such purchases could take place through several smaller contracts or, if legally facilitated, subcontracting.

Another issue is the frequent use of high, disproportionate requirements for technical and financial qualifications of tenderers. Limiting such requirements to reflect only strictly necessary preconditions, and allowing tenderers to submit joint bids, are reasonable and proportionate measures that should normally be explicitly set out in the public procurement regulations; however, they must then be more systematically applied.

Unfortunately, there is also the widespread phenomenon of late payments in the public sector. This obviously discriminates against SMEs with limited financial resources. Regulations setting strict deadlines and penalties for late payment by the public sector are a first step towards avoiding late payments to contractors, albeit not sufficient on its own.

Addressing these issues and improving public procurement practices should also be accompanied by greater attention to raising the knowledge, skill and experience levels of public procurement officials, as well as training.

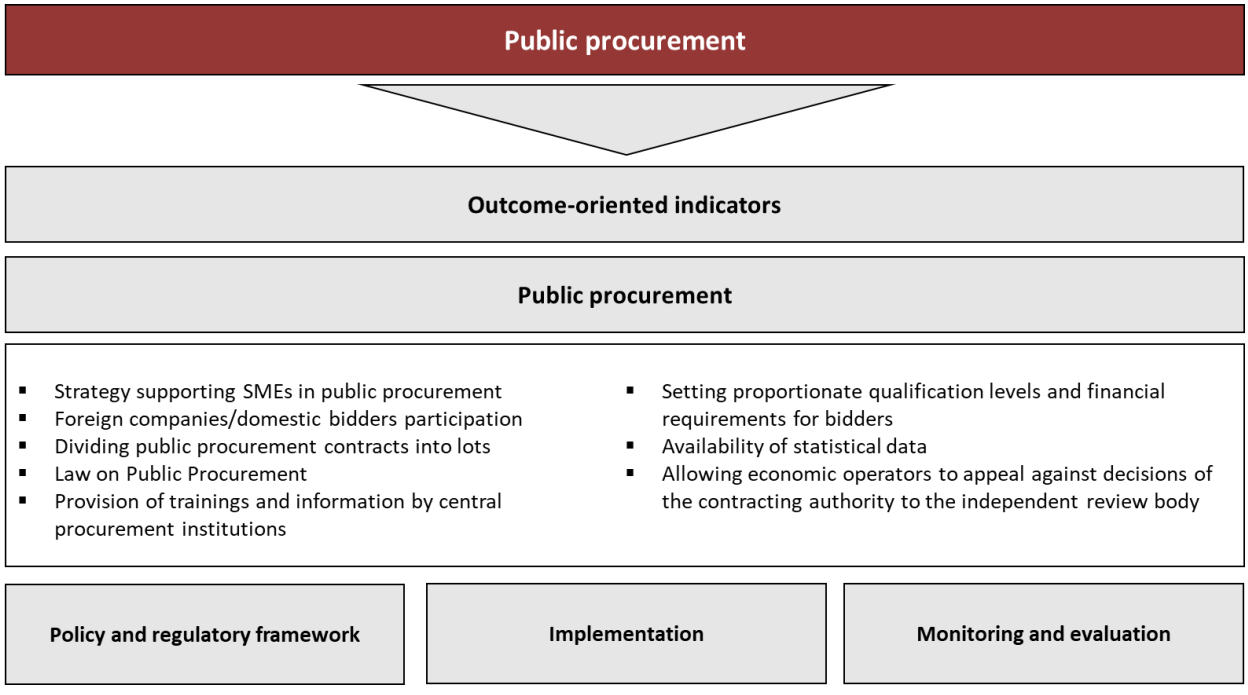
Finally, electronic procurement can help SMEs identify business opportunities; can facilitate the preparation, submission and evaluation of tenders and the management of the contracts concluded; and allows public procurement actions and outcomes to be accessed and analysed.

### *Assessment framework*

This dimension looks at policies and tools in place in EaP countries to allow SMEs better access to public procurement markets. It does so through three thematic blocks: 1) policy and regulatory framework; 2) implementation; and 3) monitoring and evaluation (Figure 8.1).

Two important methodological changes have been introduced in this dimension since the previous SBA assessment: i) the information requested has been expanded to include a set of questions on the use of a central electronic registry for public procurement and the establishment and operation of a National System of Electronic Public Procurement (NSEPP), and ii) the analysis now considers countries' ability to collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators"). The indicators selected for this dimension are: i) SMEs' share in the total value (or number) of public contracts awarded, ii) share of SMEs having taken part in a public tender/public procurement procedure, iii) success rate for participation in public procurement (by enterprise class size), iv)the share of e-procurement platform use (value of contracts submitted via the e-procurement platform over the total value of procurement contracts), v) share of SMEs submitting proposals in a public electronic tender system (e-procurement), vi) average delay in payments by public authorities, and vii) share (value and/or number) of contracts awarded to foreign economic operators.

**Figure 8.1. Assessment framework – Public procurement**

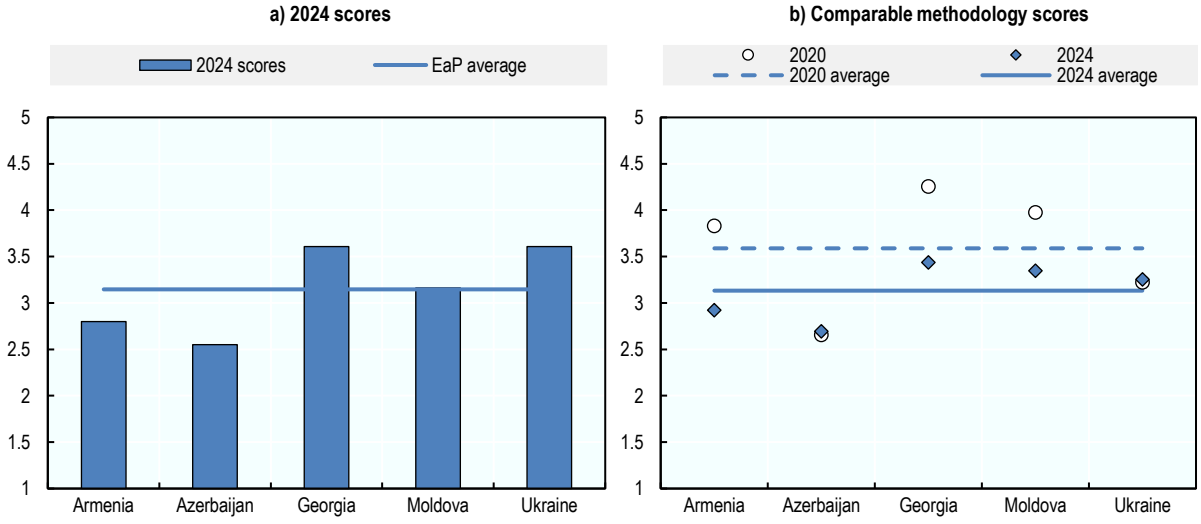


## *Analysis*

### *Regional trend and comparison with 2020 assessment scores*

The results of the SBA assessment in this dimension reveal a discernible shift in the trajectory of EaP countries' performance. While there are glimpses of progress in the areas of implementation and monitoring of public procurement policy in some countries (Azerbaijan, Moldova and Ukraine), the opposite can be observed across all countries regarding the public procurement regulatory framework. This can be attributed to a range of factors, including the absence or delay in strategic initiatives, a dearth of institutional capacity, conflicts of roles that hinder effective decision making, and the underutilisation of e-procurement systems. The combination of these issues has driven a decrease in the scores of this dimension compared to the previous assessment, with the EaP average dropping from 3.59 to 3.13 when looking at comparable methodology scores. Several recent initiatives have been taken to redraft public procurement laws, to prepare medium-term development programmes, and to improve e-procurement systems. Although it is not possible to fully reflect these initiatives in the 2024 report, they give hope for rapid improvement of future scores in public procurement.

**Figure 8.2. Public procurement, dimension score**




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/dhzj8y

### *Public procurement*

Since the assessment made for the 2020 report, public procurement in the five countries covered was heavily affected first by the COVID-19 pandemic and then by Russia's war of aggression against Ukraine. In both cases, supply chains have been upset, prices have changed rapidly, administrative procedures have had to be reorganised and urgent needs have appeared for items that were not included in earlier procurement planning.

As a result, much of the available staff resources and funds have had to be reallocated to meet these new, short-term needs. The use of less competitive procedures, as mostly provided in public procurement legislation for addressing unforeseeable, urgent needs, has increased. The generation of comprehensive, reliable public procurement data has suffered. Longer-term reform work, such as strategy development, e-

procurement enhancement and developing sustainable procurement, has often been put on the back burner. At the same time, the increased pressure to become more effective and efficient and obtain better value for money appears to have had some beneficial effects on attitudes and approaches, although evidence for this is still scarce.

The outcome of these developments is that the situation for SMEs with respect to participation in public procurement did not improve as much as expected at the beginning of the period.

Policy making has mostly focused on developing and introducing new ways of working as needed for handling the new and different needs generated by the COVID-19 pandemic and the war in Ukraine. This has mostly been done without any major changes to the public procurement laws, which were only slightly amended during the period covered. Likewise, there has been little progress in updating the medium-term strategic framework for public procurement, which is still little developed or even missing in some of the countries. In addition, there is mostly a lack of effective harmonisation between public procurement strategies (to the extent that they are in place) and strategies (if any) in other, more or less closely related fields, such as those for SME development and support, public financial management, sustainable development, civil service, administrative procedures and higher education.

Consequently, SMEs have continued to face a number of shortcomings in the regulatory framework, similar to those identified in the 2020 report. Legal provisions intended to support and facilitate SME participation would typically cover:

- free and easy access to notices, tender documents and other information
- ready availability of guidance and training
- possibilities to seek clarifications to tender documents
- rules on division into lots, joint tendering and subcontracting
- obligation for contracting authorities to set proportionate qualification requirements (administrative, technical, financial, professional, etc.) to be met by tenderers
- clear and simple rules and requirements for demonstrating conformity with the qualification requirements
- obligation for contracting authorities to pay invoices on time
- fair, transparent, timely and competent handling of complaints by an independent review body.

However, the public procurement laws are deficient in this respect, in that one or several of these provisions are incomplete or lacking in each country.

There is still room for improvement in institutional capacity, both in the central institutions at the national level and in individual contracting authorities. Skill gaps remain and the level of professionalisation is still low. Gaps, overlaps and conflicts of roles are sometimes found both within and between the institutions in charge of central functions in the public procurement system. The provision of training and guidance has improved, mainly by the increased availability of materials and tutorials accessible via the Internet. However, the focus remains chiefly on the procedural aspects of tendering and evaluation. There is room for improvement in the coverage of the preceding and subsequent steps in the public procurement cycle: planning and preparation, including needs identification, market consultations, drafting of requirements, and selection and award criteria; contract management; and monitoring and *ex post* evaluation of procurement activities.

The use of e-procurement systems has become nearly ubiquitous. However, all the methods, tools and criteria provided for in the public procurement laws are not yet fully reflected in the functionalities available in the systems in place at present. Few e-procurement systems cover more than the notification, tendering and award phases, complemented by facilities for online submission of complaints. The use of machine-readable documents is not fully implemented, leading to difficulties in accessing and analysing information (some of which has been entered using, for example, PDF files created by scanning hardcopy originals)

and to the need, in many cases, to re-enter the same data at different stages of the procedures. Progress has been made in the provision of public access to data on procurement activities, with a range of analytical functions made available to any interested parties. However, these do not always allow a full and clear picture of the actual situation, as the range of data is limited; some information is not directly readable (as just mentioned) and some transactions may be missing, particularly for small value procurement.

In practice, the purchase price remains the most-used award criterion by far, partly because of limitations in the e-procurement systems currently used, and partly because of a lack of knowledge and skills in defining and applying other criteria. As a result, quality is rarely used as an award criterion and the concept of sustainable procurement (used for lifecycle costing, for example), is difficult to apply. Many e-procurement systems also lack functions for effective and efficient application of selection criteria (reflecting grounds for exclusion and requirements for certain qualifications) at the appropriate, early stage of the evaluation process. Consequently, SMEs with innovative, efficient solutions with the potential to give good value for money in the long run, often find it difficult or impossible to compete with companies offering low purchase prices for traditional items that may have higher costs for energy, consumables, wear and spare parts.

At the level of the contracting authorities, there is slow but steady progress in filling remaining gaps in the knowledge, skills and experience of staff in charge of public procurement. These gaps are particularly prominent in two particular contexts: i) when there is a large number of small contracting authorities, each with limited resources, and ii) when public procurement is not systematically handled by specialists employed for the purpose and working in a dedicated administrative unit. Centralised purchasing and wider use of framework agreements have the potential to mitigate these issues, if well managed. They could then also help support wider SME participation. However, these approaches are still not often used, even if legal provisions for the purpose are present in the public procurement laws.

Management action in public procurement often puts the focus on securing compliance with procedural requirements and on staying within the current year's purchase budget. There is much less emphasis on properly determining the actual needs and the best way of meeting them (given what the supply market may be able to deliver) on minimising the long-term costs to the authority and to the country, and on carefully managing the contracts that have been concluded and evaluating to what extent they have provided value for money while allowing the needs to be met. Combined with the relative weakness of staff skills in procurement planning and preparation and in contract management, this again creates difficulties for agile, competent SMEs trying to compete against larger, established suppliers.

The supply markets in most of the EaP countries are fairly thin. There are sometimes only one or a few companies active in a particular industrial sector or a specific region, perhaps with close relations to the relevant authorities, and therefore with some risk of collusion or corruption in public procurement – and thus disincentives for other companies, especially SMEs, to enter the market. Even when the supply market is more diversified, SMEs may lack interest in participating in public procurement because of perceptions of costly, cumbersome procedures; disproportionate qualification requirements; or biased or unclear requirements, making it difficult to tender and to succeed. A related issue is that contracts may be for quantities or delivery conditions that can hardly be met by any individual SME. In this case, the problem may be addressed through increased use of subcontracting and joint tendering, to the extent that the legal possibilities for this exist and that contracting authorities as well as prime contractors are willing and able to take this route.

### Table 8.2. Public procurement, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.00** | **2.72** | **3.68** | **3.40** | **3.58** | **3.28** |
| Policy and regulatory framework | 2.75 | 2.43 | 3.09 | 3.75 | 3.42 | 3.09 |

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| Implementation | 4.09 | 2.83 | 4.43 | 4.20 | 3.51 | 3.81 |
| Monitoring and evaluation | 1.00 | 3.00 | 3.00 | 1.00 | 4.00 | 2.40 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### *The way forward*

To improve and encourage SME participation in public procurement, EaP countries should:

- add and improve regulations facilitating SME participation, without privileges or preferences that would distort the markets;
- strengthen central institutions' capacity for evidence-based policy making by delivering guidance and training, reviewing complaints, and monitoring system performance, all with a clear SME focus;
- improve the sequencing of e-procurement steps, add criteria other than price and make better use of e-procurement for generating and using data;
- make better use of the potential of centralised purchasing and the use of framework agreements to support wider SME participation;
- reorganise the public procurement function in contracting authorities, raise the status of procurement officers and improve their knowledge and skills; and
- inform and train SMEs as necessary for raising their trust in the system, their level of participation and their ability to get contracts to deliver and get paid.

## Standards and technical regulations

Technical regulations set out essential requirements for products before they are placed on the market. They are at the heart of national quality infrastructure[1] systems and are designed to serve legitimate public policy objectives, such as protecting health and safety or the environment. In addition, standards facilitate interoperability between different products and technologies, and promote fair competition by establishing a level playing field for businesses. Ultimately, research shows that standards can promote innovation (Blind, 2022[7]) and are trade-enhancing since they facilitate the exchange of information (Blind, 2004[8]). Bringing the legislation of EaP countries in line with the international and European framework for technical regulations and standards therefore offers substantial trade benefits, such as simpler conformity assessment procedures, shorter time to market and lower total costs of trading.

However, when the costs of adopting a standard are too high, they can act as barriers to trade (Mangelsdorf, 2011[9]; Moenius, 2004[10]; Swann, 2010[11]). Costly product standards and certification procedures, and, in particular, a lack of information about requirements in the foreign country, are the main obstacles SMEs face when attempting to enter international markets (WTO, 2016[12]). The diffusion and implementation of technical regulations and standards require relevant institutions to evaluate and confirm compliance levels, through services such as certification, testing, conformity assessment, metrology and market surveillance. Given SMEs' limited capabilities and opportunities to export, special measures may be needed to facilitate their compliance with product requirements, such as ensuring easy access to information on technical regulations, as well as opportunities to make use of reliable and efficient quality infrastructure.

### *Assessment framework*

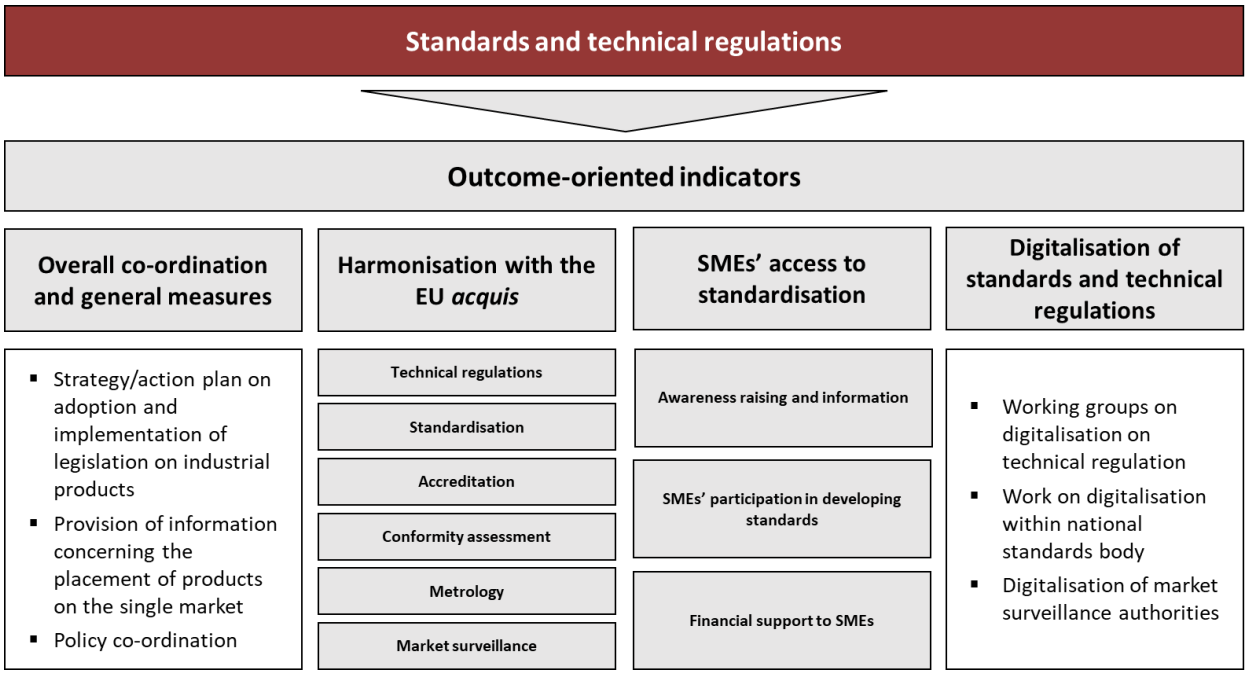
This dimension investigates whether the EaP countries have a well-functioning quality-infrastructure system and the extent to which it aligns with European Union (EU) rules and standards.

Two important methodological changes have been introduced in this dimension since the previous SBA assessment: 1) a new sub-dimension looks at efforts directed towards the digitalisation of processes within relevant authorities, as well as the introduction of remote audit and inspection activities and digital activities of surveillance authorities; 2) the analysis also considers countries' ability to regularly collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators").

The updated assessment framework considers the following (Figure 8.3):

- **Overall co-ordination and general measures:** This sub-dimension looks at general policies and tools for overall policy co-ordination and strategic approaches to adopting and implementing EU legislation. The assessment also evaluates the extent to which SMEs have access to all relevant information on requirements for exporting to the EU.
- **Harmonisation with the EU acquis:** Here, the national quality infrastructure systems is analysed with respect to six thematic blocks – technical regulations, standardisation, accreditation, conformity assessment, metrology, and market surveillance. More specifically, it analyses their institutional capacity, adoption and implementation of strategic documents, and integration into international structures. It also examines whether legislation and instruments are subject to regular monitoring and evaluation.
- **SME access to standardisation:** The third sub-dimension evaluates government efforts to increase SMEs' awareness of standards and facilitate their participation in developing them. It also considers the availability and scope of current financial support programmes aimed at enhancing the implementation of standards among the SME population.
- **Digitalisation of standards and technical regulations:** This evaluates support and training offered to SMEs on standards and technical regulations for their integration into the EU Digital Single Market; the digitalisation of processes within authorities responsible for technical regulation, national standards and accreditation bodies, metrology institutes, and market surveillance authorities; and the introduction by accreditation bodies, conformity assessment bodies (CABs), and surveillance authorities of remote audit and inspection activities.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information about the following indicators: i) share of the total exports directed to the EU Single Market, ii) percentage annual growth of exports to the EU Single Market, and iii) share of manufactured products in total exports to the EU Single Market.

## Figure 8.3. Assessment framework – Standards and technical regulations

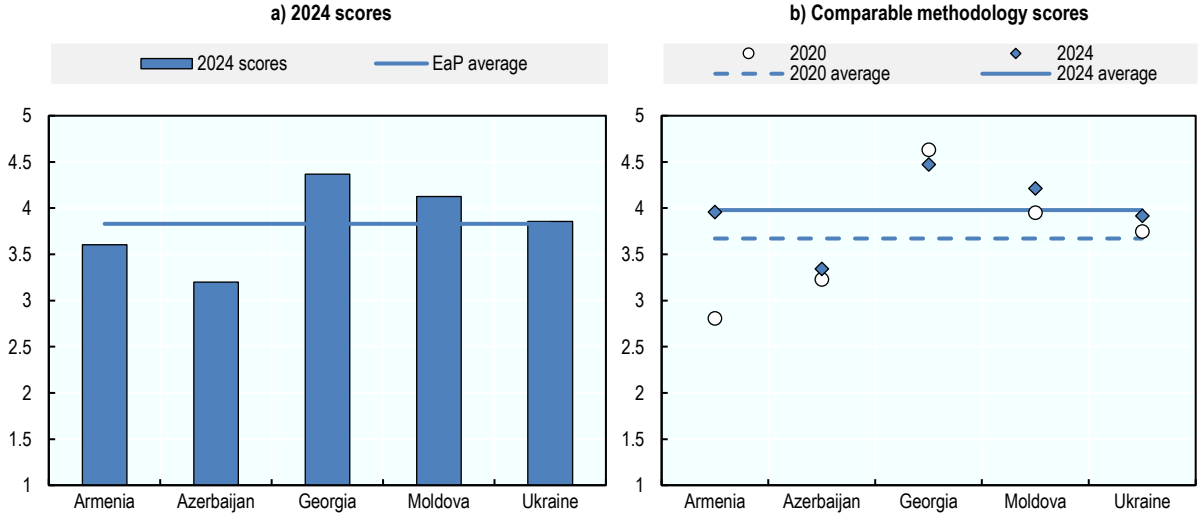



### *Analysis*

*Regional trend and comparison with 2020 assessment scores*

The EaP region has progressed in the field of standards and technical regulations, reaching an average score of 3.83 (Figure 8.4). All countries have worked intensively on this dimension, and this is reflected by higher scores for most countries (Armenia, Azerbaijan, Moldova and Ukraine); Georgia remaines the clear leader in this dimension.

## Figure 8.4. Standards and technical regulation, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### *Overall co-ordination and general measures*

All countries have a designated government body responsible for the overall co-ordination of technical regulations and quality infrastructure (QI). By contrast, the current development stages of this sub-dimension's other areas vary. Armenia, Georgia and Ukraine recorded the highest scores, but progress was also visible in Moldova, which reached a score above 4, and in Azerbaijan.

Armenia could answer positively on all questions of this dimension. Georgia conducted significant reforms in the market surveillance system for non-food products. Establishing the independent Market Surveillance Agency (MSA) was a major step in this context. Likewise, Ukraine worked continuously on reforms to promote a favourable business environment and regulatory framework; the Entrepreneurship and Export Promotion Office (EEPO) was created as a single contact point for SMEs. As a specific highlight, Ukraine has progressed in its negotiations with the EU on Agreements on Conformity Assessment and Acceptance of Industrial Products (ACAA).

A key accomplishment of Moldova was the amendment of Law 420/2006 on technical regulation in 2020, which brought the country's technical regulation in line with the provisions of the World Trade Organisation (WTO) Technical Barriers to Trade (TBT) Agreement. Likewise, Azerbaijan progressed in aligning its national legislation with WTO requirements. Progress was also visible in its institutional framework for market control and standardisation. In addition, an action plan for the adoption and implementation of (EU) legislation on industrial products is under preparation.

Current Azeri legislation associates "market surveillance" mainly with inspections, but various market monitoring activities have also taken place. Businesses involved in export can obtain all the required certificates from the "One-Stop Shop" Export Support Centre. In addition, azexport.az provides information on Azeri products to support their foreign sales. However, as in Moldova, further efforts are needed to develop an online portal or a specific portal for SMEs containing all the relevant information concerning the export of products to the EU Single Market.

**Table 8.3. Overall co-ordination and general measures, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **5.00** | **3.23** | **5.00** | **4.33** | **5.00** | **4.51** |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### *Harmonisation with the EU acquis*

The second sub-dimension, harmonisation with the EU *acquis*, is multi-dimensional and led by Georgia, closely followed by Ukraine. Its first thematic block refers to technical regulations. Four countries (Armenia, Georgia, Moldova, and Ukraine) reached scores above 4. All these countries have an action plan or similar on transposing EU sectoral legislation in priority sectors. Ukraine has created an action plan for developing the technical regulation system. Likewise, it has adopted legislation to align itself with the EU acquis on various products and is awaiting the EU's verification. Another example of progress in this block is Armenia's implementation of a roadmap on transposing EU sectoral legislation in priority sectors. Georgia adopts annual action plans for Deep and Comprehensive Free Trade Agreement (DCFTA) implementation, where approximation (i.e., alignment) with the EU sectoral legislation in priority sectors is prescribed. Although Azerbaijan attained a lower score than the other countries, progress was also visible. In particular, it amended legislation based on WTO principles and requirements. An action item for the whole region is the regular evaluation of technical regulations.

In the second thematic block (standardisation), Armenia, Georgia and Moldova reached scores higher than 4, and the other countries scored at least 3. Georgia's, Moldova's, and Ukraine's standards bodies were granted CEN and CENELEC Affiliate status; this was approved in 2022 and entered into force in January 2023. Except for Azerbaijan, the adoption rate of EU standards is at least 50% in priority sectors. Azerbaijan approved the new State Programme "On the harmonisation of the national standardisation system in accordance with international requirements for 2023-2025" at the end of the current SME Policy Index period.

Other examples of progress in this thematic block are Armenia's annual state standardisation programmes (introduced in 2020) and Ukraine's strategy for integration into the EU Single Digital Market (with a focus on telecommunication regarding standardisation). Likewise, Azerbaijan used support from Germany to implement the National Plan for harmonising the national standardisation system with international requirements.

Results on standardisation education varied. Three of the five countries (Armenia, Georgia and Moldova) have a targeted strategy. Georgia also started creating an e-learning platform. Moldova has an "Activity Strategy" for 2021-23 that is focused on education projects and works on the establishment of a standardisation academy. Training events regularly organised by the Institute for Standardisation of Moldova (ISM) help to stimulate the implementation of new standards. Nevertheless, Armenia and Georgia are the only countries whose standardisation education strategy also considers SME-specific aspects. Education on standardisation thus remains an action item for the region.

Regarding the third thematic block (accreditation), all countries reached scores of close to 4 or higher. All countries have accreditation bodies, although only those of Georgia and Moldova have been completely positively assessed by the European Co-operation for Accreditation (EA) or by peer organisations. Another accomplishment was that in 2022 Georgia's accreditation body, the Georgia Accrediting Commission (GAC), became a full member and signatory of the Mutual Recognition Arrangement (MRA) of the International Laboratory Accreditation Cooperation (ILAC) and the Multilateral Recognition Arrangement (MLA) of the International Accreditation Forum (IAF).

In thematic block 4 (on conformity assessment), Georgia, Moldova and Ukraine reached scores above 4, and Armenia and Azerbaijan of around 3. Azerbaijan does not have legislation on conformity assessment in line with the *acquis*. Likewise, Armenia's legislation is not totally in line with the *acquis*, which also influences its specific conformity assessment activities. Conformity assessment bodies in line with EU requirements exist in Ukraine's priority sectors. Georgia and Moldova have such bodies in most priority sectors. They are the only countries in the group with SME-designated web pages with information on conformity assessment bodies. Also in this dimension, regular evaluation is an action item for the whole region.

The fifth thematic block of this sub-dimension is metrology. Armenia, Georgia and Ukraine reached scores above 4, with Armenia and Ukraine close to 5. All countries have an operational metrology body, although only Armenia, Georgia and Ukraine also have a strategy for metrology. In this context, the Georgian National Agency for Standards and Metrology (GEOSTM) became an associate member of EURAMET in 2022, and preparations to become a full member are under way.

Most of the five countries have legislation on metrology in line with the *acquis*, while Azerbaijan is preparing a proposal for such legislation. Further alignment of Ukraine's metrology centres with the *acquis* is also necessary, although relevant legislation is in place. Besides creating the National Body for Standards and Metrology (ARMSTANDARD), Armenia has developed a Programme on the Development of Metrology and a List of Measures for 2020-2023; however, Armenia's national metrology institute does not envisage recognition by relevant international/European organisations. Progress was also visible in Azerbaijan and Moldova. In this context, Moldova initiated the re-organisation of its National Institute of Metrology and visible results can be expected soon.

Results of the sixth thematic block (market surveillance) are mixed. Georgia scored the best, at 4.60, followed by Ukraine with a score of slightly more than 4. Georgia progressed in various fields, mainly as part of overall co-ordination measures (see above). It has also introduced a new online market surveillance database. In Ukraine, certain market surveillance measures are in place and others are being developed. A strategy for market surveillance is also under development.

Azerbaijan and Moldova reached scores of around 3, while Armenia's score was lower. In this context, Moldova established the State Inspectorate for the Supervision of Non-Food Products and Consumer Protection based on the reorganisation of the Agency for Consumer Protection and Market Surveillance. Azerbaijan's State Agency for Antimonopoly and Consumer Market Control was placed under the Ministry of Economy.

### Table 8.4. Harmonisation with the EU *acquis*, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **3.58** | **3.30** | **4.42** | **3.94** | **4.40** | **3.93** |
| Technical regulations | **4.10** | **3.14** | **4.36** | **4.10** | **4.42** | **4.02** |
| Standardisation | 4.25 | 3.30 | 4.49 | 4.05 | 3.67 | 3.95 |
| Accreditation | 3.61 | 3.84 | 4.36 | 4.36 | 4.80 | 4.19 |
| Conformity assessment | 2.76 | 3.40 | 4.19 | 4.29 | 4.68 | 3.87 |
| Metrology | 4.78 | 3.35 | 4.47 | 3.80 | 4.73 | 4.23 |
| Market surveillance | 1.94 | 2.76 | 4.60 | 3.00 | 4.04 | 3.27 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *SME access to standardisation*

The third sub-dimension, SMEs' access to standardisation, starts with the thematic block on awareness raising and information. With Moldova and Armenia at the top, all countries achieved good or very good results in this block with scores between almost 4 and 5. All countries have measures in place to increase SMEs' awareness of standards and have conducted promotional campaigns on standards.

Regarding mentoring programmes to guide SMEs through standardisation activities, Moldova's Institute for Standardisation and the Organisation for Entrepreneurship Development signed a collaboration agreement to provide support and professional assistance to familiarise SMEs with standardisation and promote the participation of SME representatives in the work of technical committees of the Institute for Standardisation. Azerbaijan initiated more than 70 training events and meetings in 2022.

In the sub-dimension's second thematic block, SME participation in developing standards, the results (led by Moldova, Armenia and Georgia) vary between 3.50 and 5. As a good practice example, Armenia has a working group that assesses SME needs and provides appropriate services and information. A recent example of the involvement of SMEs in standardisation was the formulation of requirements for berries in a fruit product.

With Moldova and Georgia on top, the figures of the third thematic block (financial support to SMEs) show the biggest spread in this sub-dimension with scores between 1.5 and 4. They are also the lowest of this sub-dimension, indicating a need for action.

Moldova supports SMEs' purchase of standards and participation in the development of standards by various financial and non-financial measures; there are also two new State Programs that promote the implementation of international standards and and certification (e.g. through business vouchers). Likewise, Georgia's National Standardisation Strategy for 2022-2024 improved the availability of standards for SMEs

and stimulated their participation in standardisation activities. A 10% discount rate for SMEs for purchasing standards was adopted by the Ordinance of Government of Georgia No. 503 in 2022.

In Armenia, ARMSTANDARD provides specific financial conditions for acquiring standards for SMEs. Between 2018 and 2021, almost 30 SMEs annually benefitted from various financial support schemes to improve their access to standardisation. Likewise, financial support to acquire standards is available in Azerbaijan. Ukraine provides a loyalty program for industry associations with a 5-10% discount depending on the volume of ordered standards, but SMEs are not considered specifically in this context.

### Table 8.5. SME access to standardisation, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **3.85** | **3.25** | **4.13** | **4.55** | **2.83** | **3.72** |
| Awareness raising and information | 4.33 | 4.17 | 4.25 | 4.83 | 3.92 | 4.30 |
| SMEs' participation in developing standards | 4.50 | 4.00 | 4.50 | 5.00 | 3.50 | 4.30 |
| Financial support to SMEs | 3.00 | 2.00 | 3.75 | 4.00 | 1.50 | 2.85 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

#### *Digitalisation of standards and technical regulations*

The fourth sub-dimension, digitalisation of standards and technical regulations, is characterised by relatively low scores on average. Georgia leads the ranking with a score of 3.63, followed by Moldova and Ukraine, and finally, with scores around 2, Azerbaijan and Armenia.

In Georgia, GEOSTM has synchronised and harmonised the national standards database with those of CEN and CENELEC. It also started updating its internal procedures in parallel with the development of the last SME Policy Index report. Georgia began to digitalise its accreditation services in 2021 and expected its digital system to become fully operational in mid-2023.

Moldova's ISM implemented the standard SM EN ISO 22301 in response to the COVID-19 pandemic, which also led to the digitalisation of several SME-related processes and is a good starting point for further digitalisation. Ukraine has an action plan for 2023 to digitalise public services.

Armenia has a digitalisation strategy to ensure the digital transformation of the government, economy and society. Its Ministry of High-Tech Industry has developed a digitalisation toolkit that is to be adopted by the country's technical regulatory authorities.

Azerbaijan's State Committee on Standardisation, Metrology and Patents (AZSTAND) introduced a standards document management system and an electronic sales platform at the end of the current assessment period. Likewise, the country has a plan for digitising its metrology institute. The further digitalisation of the country's quality infrastructure should also include a strategy or action plan for digitising the national accreditation body.

Most countries offer support and training to SMEs on standards and technical regulations for their integration into the EU Digital Single Market. Likewise, most countries have strategies for the digitalisation of processes within the authorities responsible for technical regulation.

However, work remains to be done. Designated staff or special working groups for the digitalisation of processes and activities within the area of technical regulation are missing in almost all the countries. Only Georgia is more advanced in this context. In addition, digitalisation is partly considered in Moldova's standardisation strategy. Except for Armenia and Azerbaijan, remote participation in standardisation is

possible in the region. Georgia is also one of the two countries (together with Ukraine) with a digitalisation strategy for its accreditation body.

Remote audit and inspection are particularly practiced by Georgia's and Moldova's accreditation bodies, although no country provides this service for first-time accreditation. Specific action items in the region refer to remote audit, inspection and calibration activities by conformity assessment bodies.

Except in Georgia, the digitalisation of market surveillance is still underdeveloped in the region.

### Table 8.6. Digitalisation of standards and technical regulations, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **1.50** | **2.13** | **3.63** | **2.50** | **2.50** | **2.45** |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

### *The way forward*

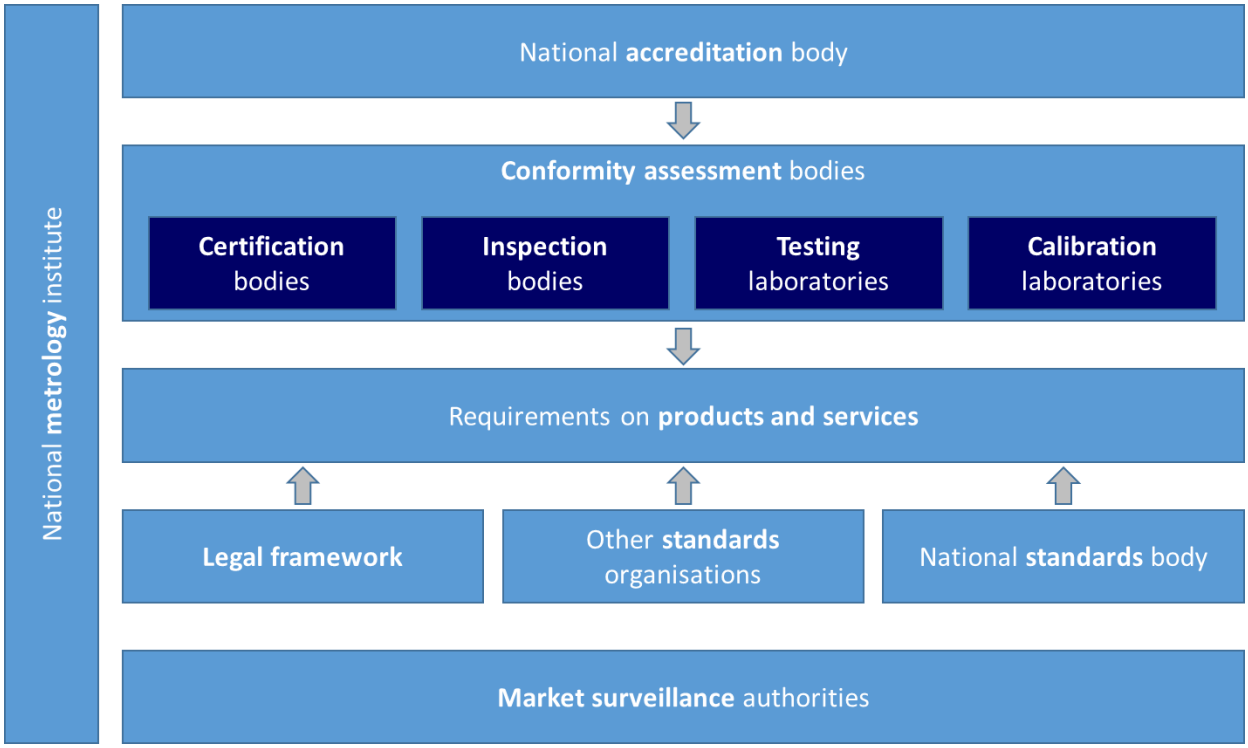
Based on these analyses, EaP countries should:

- **Improve the quality infrastructure's market surveillance dimension and intensify understanding of market surveillance (and how it differs from inspection).** As the Policy Index shows, the market surveillance score is the lowest of the "Harmonisation with the EU a*cquis*" sub-dimension and lower than in 2020. Various reorganisations regarding market surveillance took place in the region and implementing appropriate surveillance measures paired with digitalisation will be important next steps. In addition, differentiating between inspection and market surveillance is important to maximise the impact of both instruments. Figure 8.5 shows their differences, with inspection being part of conformity assessment and market surveillance a separate quality-infrastructure element.
- **Take further steps for quality infrastructure to be internationally recognised.** This recommendation mirrors the recommendation made to Armenia and Azerbaijan in 2020 but is also relevant for the other countries. A specific accomplishment in this context was that Georgia's accreditation body, the GAC, became a full ILAC member in 2022. Other relevant collaborations worth seeking include, for example, the International Accreditation Forum (IAF) and bilateral agreement (BLA) with the European co-operation for Accreditation (EA).
- **Develop standards education strategies (further) by considering SME-specific aspects.** Overall education in the area of standardisation has become a high priority on the European Commission's agenda – for example, in the EU's 2022 standardisation strategy. However, the results on standards education vary. Besides the existing approaches in the region to learn from in Armenia, Georgia and Moldova, the EU addresses standards education also by the HORIZON-EUROPE measure "Provide for a strong and sustainable pool of experts for European standardisation." Connecting with the measure's project(s) might be beneficial to profit from the relevant results.
- **Develop financial measures to further support SME participation in standardisation.** A comparable recommendation was also given in the 2020 report. Currently, the thematic block on financial measures has the lowest score besides the new dimension on digitalisation. Although progress since the 2020 assessment is apparent, it is important to continue implementing appropriate SME support measures in this area.
- **Improve the digital maturity of the technical regulation system and quality infrastructure, especially in the field of conformity assessment.** The new sub-dimension on digitalisation has the lowest average score (2.45). Action is needed in this area, in particular in the field of conformity

assessment. Germany's Federal Institute for Materials Research and Testing (BAM) and its international partners in 15 countries worldwide[2] conducted a multinational analysis on the digitalisation of this quality infrastructure element. Various recommendations were made with broader relevance. While the EaP countries were not part of the study, the analysis of nearby Latvia[3] provides useful insights.

- **Provide export platforms specifically considering SMEs' trade with the EU where none exist.** There are various web-based export tools in the region, but their support for SMEs and their trade with the EU varies. This has to be improved. Based on the already established ties between the relevant organisations and their dedicated work to support SMEs, this recommendation seems to be easy to accomplish. The region's work on digitalisation can provide additional support for these efforts.
- **Improve the regular evaluation of the technical regulation system and quality infrastructure by specifically considering areas *without* and *without regular* evaluation.** The evaluation of the technical regulation system and QI, which was already addressed in the recommendations of the last assessment, still varies significantly regarding frequency, clear responsibilities and the way the evaluation has been conducted. Since the collection of SME data and surveys may be resource-consuming, it should also be investigated to what extent collaborations with universities/PhD schools might help to collect data and analyse the effects of QI-specific measures.
- **Continue with good practice of Twinning projects after their completion.** The EaP countries have used various Twinning projects that have supported the countries in many areas, for example regarding evaluations. It is important to consolidate the good practice of the projects and to specify responsibilities for continuing the helpful measures even after the projects end.

### Figure 8.5. Quality infrastructure elements




Source: (Blind and Koch, 2017[13]).

## SME internationalisation

Given the relatively small size of EaP countries' domestic markets, combined with pressure from international competition, access to foreign markets is crucial to SMEs' long-term viability. Besides opening new markets, the internationalisation of SMEs and their participation in GVCs exposes them to international competition and helps them achieve economies of scale. This can, in turn, enable SMEs to enhance productivity by capturing technology and knowledge spillovers, upgrading workforce and managerial skills, and raising innovation capacity (OECD, 2023[3]).

As digital transformation progresses, e-commerce opens new opportunities for SMEs to enter foreign markets at a relatively low cost. In fact, through online platforms, SMEs can overcome geographical barriers and increase their market reach while lowering marketing and distribution costs, including delivery, payments and marketing costs (Jahanshahi, Zhang and Brem, 2013[14]). Furthermore, the COVID-19 pandemic accelerated the expansion of e-commerce and has demonstrated the importance of digitalisation and its contribution to growth and development (OECD, 2020[15]).

However, SMEs face several challenges in accessing foreign markets, integrating into GVCs and adopting e-commerce practices. Expanding into foreign markets demands substantial investments in research, marketing and logistics, and SMEs often lack the necessary financial and human resources. Cultural and language barriers add to the difficulty, impeding effective communication with potential customers and partners. In addition, in the realm of e-commerce, digital infrastructure and skills are vital (see the Digital Economy for SMEs chapter). SMEs must also address cybersecurity concerns and data protection to mitigate risks associated with online transactions (European Union, 2021[16]).

Against this background, helping SMEs to enter international markets – and to be competitive in them – requires a whole-of-government approach that addresses the constraints that SMEs face in internationalising, including access to information, skills, technology and finance, as well as trade facilitation and connectivity (OECD, 2019[17]). Governments should make an effort to remove barriers to trade and reduce the cost and complexity of trade procedures.

Furthermore, targeted government support for SMEs in export promotion, integration into GVCs and e-commerce can facilitate the internationalisation of SMEs and propel their integration into the global economy. This includes financial services for exporting SMEs, and training and consultancy services to increase SME readiness for internationalisation.

### *Assessment framework*

This dimension assesses governments' support for export-oriented SMEs.

Two important methodological changes have been introduced in this dimension since the previous assessment: 1) the sub-dimension on the use of e-commerce has been substantially expanded to better capture policies in support of businesses' access to hybrid retail opportunities; and 2) the analysis now considers countries' ability to regularly collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators").

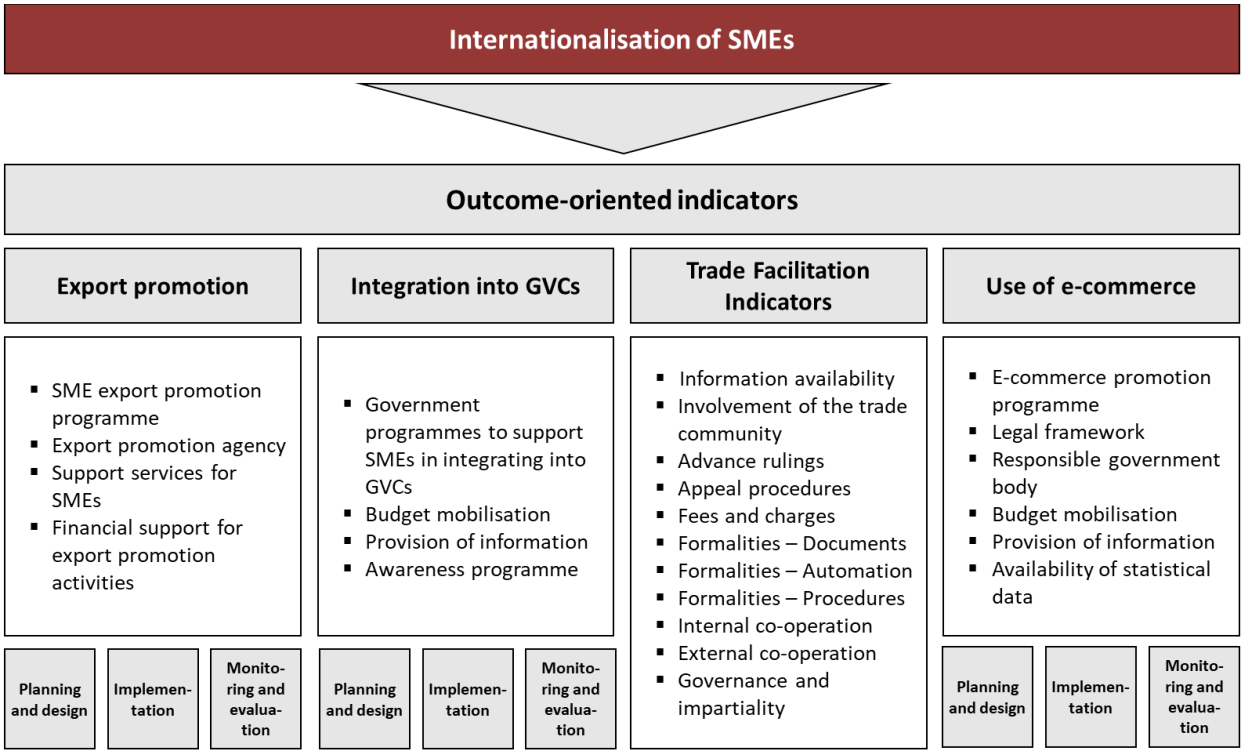
The assessment framework considers the following (Figure 8.6):

- **Export promotion:** The first sub-dimension looks at approaches to export support, promotion activities and government support services for SMEs with export potential. It focuses on the existence of export promotion strategies and the role and activities of export promotion agencies, and examines the level of monitoring and evaluation of existing export promotion programmes.
- **SME integration into GVCs:** The second sub-dimension analyses the extent to which governments support the integration of local SMEs into GVCs by examining the availability of government programmes supporting cluster development, the creation of supply chain linkages

between SMEs and multinational enterprises (MNEs), and the transfer of human capital and technology from MNEs.

- **OECD Trade Facilitation Indicators (TFIs):** Here, the set of measures that streamline and simplify the technical and legal procedures for products entering or leaving a country to be traded internationally is assessed.
- **Use of e-commerce:** This sub-dimension investigates efforts towards encouraging more widespread use of e-commerce as a sales channel by SMEs, considering both regulatory aspects and government policies to promote SMEs' access to digital platforms and the provision of support services to remove barriers that prevent SMEs from benefiting from growing trade digitalisation.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability to regularly collect statistical information about the following indicators: i) share of exporters (by size class), ii) export value to turnover ratio (by size class), iii) share of businesses making e-commerce sales that sell across borders, and iv) ICT goods and services as a share of exports.

### Figure 8.6. Assessment framework – Internationalisation of SMEs



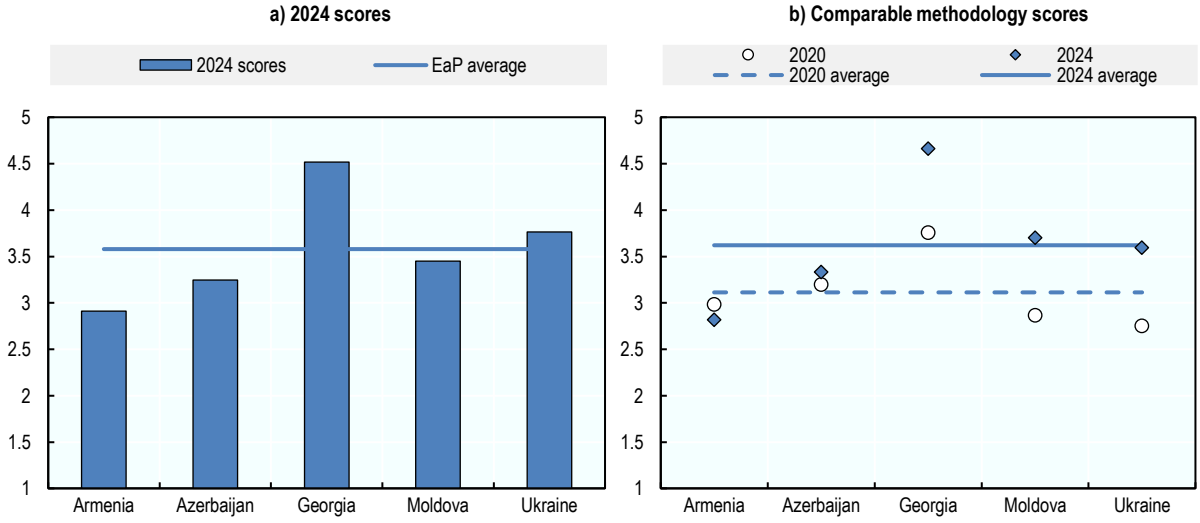

## *Analysis*

### *Regional trend and comparison with 2020 assessment scores*

The results of the SBA assessment show that all EaP countries recognise the importance of SME internationalisation and have adopted a strategic approach to export promotion and the use of e-commerce. However, the extent to which measures are well-designed and systematically implemented and measured varies significantly across countries, as shown by the high variation of the scores for this dimension (Figure 8.7).

With the exception of Armenia, all countries improved their performance with respect to the 2020 assessment. All countries' performance in the 2022 OECD Trade Facilitation Indicators has also improved with respect to the previous update in 2019.

## Figure 8.7. SME internationalisation, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### *Export promotion*

Overall, export promotion is a dimension where EaP countries perform well, obtaining an average score of 4.13 (Table 8.7). This reflects the efforts countries have made in adopting and implementing policy initiatives to promote export among SMEs.

## Table 8.7. Export promotion, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **3.57** | **3.67** | **4.84** | **4.28** | **4.30** | **4.13** |
| Planning and design | 3.90 | 4.50 | 4.75 | 4.75 | 4.80 | 4.54 |
| Implementation | 3.62 | 3.92 | 4.85 | 3.92 | 3.77 | 4.02 |
| Monitoring and evaluation | 2.89 | 1.64 | 5.00 | 4.27 | 4.64 | 3.69 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Export promotion programmes remain the main form of support for SME internationalisation in EaP countries. Bodies in charge of such programmes are usually SME agencies (Enterprise Armenia, KOBIA, Enterprise Georgia, ODA), investment promotion agencies (AZPROMO and Invest Moldova), and dedicated departments within the Ministry of Economy (Armenia and Ukraine). In Ukraine, the EEPO serves both as a business support agency and an investment promotion agency. Further support is available through export insurance agencies, such as the Export Insurance Agency of Armenia (EIAA) and the Ukrainian Export Credit Agency (ECA).

While there are currently not any active export strategies in any of the EaP countries, most of them have adopted other relevant strategic policy documents. In Armenia and Georgia, objectives related to export promotion are included in the respective SME strategies. “Diversifying and supporting growth of non-hydrocarbon exports” is one of the main directions outlined in the Implementation Plan of the 2022-2026 Socio-economic Development Strategy of Azerbaijan. In Moldova, although the two cornerstone policy documents supporting SME internationalisation expired in 2020, “Strengthening SMEs’ competitiveness and improving market access” is one of the main objectives of the draft National Program for Promoting Entrepreneurship and Increasing Competitiveness for 2023-2027 (PACC), which is to be approved in 2023. In Ukraine, before the beginning of Russia’s full-scale invasion, the government conducted a business survey to inform the update of the Export Strategy of Ukraine, which expired in 2021.

As in 2020, support is still centred around facilitation of trade missions and SME participation in trade fairs. Other promotion activities commonly offered are information support and consultancy and advisory services, trainings, and the organisation of matchmaking events and buyer missions. There are some forms of financial support to exporting companies in each of the countries. Such measures differ in their complexity and range from financing SME participation in exhibitions and fairs (offered by all countries) to more advanced mechanisms such as grant schemes and business vouchers (Moldova). In addition to support services directly provided by EaP countries, businesses in Armenia and Azerbaijan can also access advice and support offered within the framework of the Enterprise Europe Network (EEN).[4]

### Table 8.8. Overview of frameworks for SME export promotion in EaP countries

| Country | Policy documents | Agencies | Main programmes and initiatives |
|---|---|---|---|
| Armenia | SME Development Strategy 2020-2024 | Enterprise Armenia<br>Ministry of Economy or Armenia<br>Export Insurance Agency | Investment and Export Promotion Programme |
| Azerbaijan | Implementation Plan of the 2022-2026 Socio-economic Development Strategy of Azerbaijan | AZPOMO<br>KOBIA | Several scattered initiatives [1] |
| Georgia | SME Development Strategy of Georgia for 2021-2025 | Enterprise Georgia (Export Division) | Export Assistance Programme |
| Moldova | Draft National Program for Promoting Entrepreneurship and Increasing Competitiveness for 2022-2026 (PACC) [2] | ODA<br>Invest Moldova | State Program for SMEs Growth and Internationalization |
| Ukraine | Export Strategy of Ukraine 2017-2021 [3] | Ministry of Economy of Ukraine<br>Entrepreneurship and Export Promotion Office (EEPO)<br>Export Credit Agency (ECA) | Diia |

[1] No structured programme but several activities are carried out. [2] To be approved. [3] Expired.
Source: SBA Assessment questionnaire 2024.

To enhance the effectiveness and accountability of existing export promotion programmes, EaP governments should establish or improve a comprehensive system for monitoring and evaluation. While Georgia, Moldova and Ukraine are leading the way in this area, with established monitoring mechanisms in place for export promotion programmes as well as for the export promotion agency itself, Armenia and Azerbaijan are still lagging behind and have yet to introduce basic monitoring practices.

#### *Integration of SMEs in global value chains*

SMEs typically access GVCs through supply chain linkages, involving the purchase and sale of intermediate goods or services, often by supplying MNEs operating locally. Governments can play a key role in providing information and matchmaking services to fill the informational gap between SMEs and

MNEs and encourage MNEs to engage with SMEs, e.g. through tax credits for investments providing tangible benefits to local suppliers, or through concessionary financing of strategic activities.

Policy frameworks and initiatives to support SME integration into GVCs are still at a very early stage in all EaP countries, with the exception of Georgia (Table 8.9). In Armenia, Moldova and Ukraine, although no systematic support is provided, proposals in this direction have been presented. In Moldova, the above-mentioned "Strengthening SMEs' competitiveness and improving markets' access" objective of the Draft National Programme for Promoting Entrepreneurship and Increasing Competitiveness 2022-2026 (PACC), relies on several actions, including supporting SME clustering through the Support Program for Clustering Initiatives. Moreover, the Ministry of Economy and ODA are in the process of developing a local supplier programme focused on building links between domestic manufacturing SMEs and international buyers, including MNEs. In Ukraine, in 2020, the Cabinet of Ministers adopted a resolution on the approval of a state programme to stimulate the economy in the aftermath of COVID-19, which includes finding opportunities for exporters to integrate into GVCs as one of its objectives. The programme also targets the development of innovative systems, including the transfer of technologies, and the simplification of hiring procedures for foreign highly qualified workers. Unfortunately, the programme is currently not operational. However, many of the activities carried out under the *Diia.Business* project and by EEPO are helping SMEs become part of the global networks of production and trade and have led several partnerships between Ukrainian and foreign businesses. In addition, regular assessments of GVCs in different sectors are carried out to help businesses identify export opportunities.

Azerbaijan and Georgia already provide some form of support for SMEs' integration into GVCs, albeit to different degrees, mostly focused on cluster development. In Azerbaijan, although there are no comprehensive and structured programmes, eligible SMEs can apply for substantial exemptions from different types of taxes for seven years. Georgia is at the forefront with regards to cluster development support. The government carries out regular GVC assessments to understand the main opportunities for SMEs in the country. The Ministry of Economy and Sustainable Development (MoESD) and Enterprise Georgia, in co-operation with GIZ and under the EU-funded Clusters4Development Project, have developed a Cluster Policy Framework to create a beneficial cluster landscape. In addition, the Georgian Economic Security Program 2019-2024 (GESP) supports economic sectors with the highest long-term potential, helps develop value chains, enhances the viability of SMEs, supports a more skilled workforce, and facilitates public-private partnerships.

### Table 8.9. Integration of SMEs into GVCs, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **1.23** | **2.16** | **4.80** | **2.77** | **3.76** | **2.94** |
| Planning and design | 1.65 | 2.22 | 4.63 | 2.19 | 4.69 | 3.08 |
| Implementation | 1.00 | 2.33 | 4.83 | 2.83 | 3.67 | 2.93 |
| Monitoring and evaluation | 1.00 | 1.67 | 5.00 | 3.67 | 2.33 | 2.73 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

To advance in the area of support for SME integration into GVCs, EaP countries could consider carrying out regular assessments of GVCs to identify sectors with high potential and uncover new market opportunities, allowing for informed decisions on direct support to SMEs. Policymakers could support businesses to import and facilitate the establishment of links with MNEs to foster technology transfers and promote the exchange or movement of highly skilled workers. Finally, EaP countries could expand support for integrating into GVCs beyond cluster development – by, for example, expanding incentives for foreign

direct investment (FDI) to further enhance MNE-SME linkages and capitalise on the resulting spill-over of technology and financial resources.

### *OECD Trade Facilitation Indicators*

The OECD TFIs were added to the assessment framework in 2020 as a sub-dimension to capture the extent to which countries have introduced and implemented trade facilitation measures.

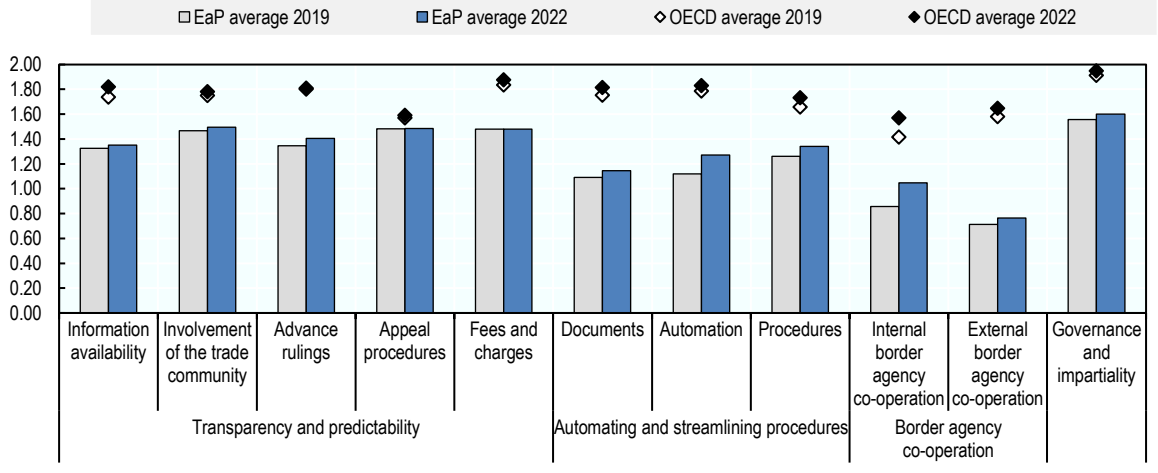
The 2022 OECD TFIs (Table 8.10) show that the implementation of measures to ease business access to foreign markets is under way and has improved over time, although the performance gap with OECD countries persists. All EaP countries have improved their performance across all 11 areas assessed since the previous assessment in 2019, and the regional average increased from 1.24 to 1.31 (on a scale from 0 to 2). At the same time, the OECD average increased from 1.71 to 1.76 in 2022, resulting in a stable gap between EaP and OECD countries of 0.46 points (Figure 8.8).

## Table 8.10. OECD Trade Facilitation Indicators, scores by country (2022)

| | ARM | AZE | GEO | MDA | UKR | EaP average |
|---|---|---|---|---|---|---|
| Information availability | 1.57 | 1.52 | 1.62 | 0.95 | 1.10 | 1.35 |
| Involvement of the trade community | 1.14 | 1.29 | 1.88 | 1.50 | 1.67 | 1.50 |
| Advance rulings | 1.67 | 1.33 | 1.46 | 1.57 | 1.00 | 1.41 |
| Appeal procedures | 1.75 | 1.25 | 1.23 | 1.56 | 1.63 | 1.48 |
| Fees and charges | 1.85 | 1.39 | 1.50 | 1.08 | 1.58 | 1.48 |
| Documents | 1.38 | 1.00 | 1.89 | 0.67 | 0.78 | 1.14 |
| Automation | 1.36 | 1.39 | 1.69 | 1.00 | 0.92 | 1.27 |
| Procedures | 1.52 | 1.46 | 1.62 | 1.30 | 0.80 | 1.34 |
| Internal co-operation | 0.91 | 1.09 | 1.73 | 1.00 | 0.50 | 1.05 |
| External co-operation | 0.82 | 0.91 | 1.09 | 0.36 | 0.64 | 0.76 |
| Governance and impartiality | 1.89 | 1.67 | 2.00 | 1.22 | 1.22 | 1.60 |
| **Country average** | **1.44** | **1.30** | **1.61** | **1.11** | **1.08** | **1.31** |

Note: TFIs take values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade facilitation indicators, https://oe.cd/tfi.

## Figure 8.8. OECD Trade Facilitation Indicators, EaP and OECD averages (2022)




Note: TFIs take values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade facilitation indicators, https://oe.cd/tfi.

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The widest performance gaps between EaP and OECD countries are in the areas of *Documents* and *Internal* and *External border agency co-operation*. In general, EaP countries should prioritise interventions in the areas of *Automating and streamlining procedures*. They should improve harmonisation and simplification of trade-related *documents*, in accordance with international standards, advance in the *automation* of procedures (e.g. by adopting electronic exchange of data and using automated risk management); and streamline *procedures* related to border control (inspections, clearance), for example, by implementing single trade windows or certified trader programmes. Finally, they could focus on *Internal and external border agency* co-operation by putting in place or improving institutional frameworks, mechanisms and IT systems for domestic co-operation between various border agencies and for co-operation of domestic border agencies with those of neighbouring economies and other trading partners.

### *Use of e-commerce for hybrid retail*

All EaP countries improved their performance on the sub-dimension dedicated to policies and provisions in place to regulate and encourage more widespread use of e-commerce by SMEs, obtaining an average score of 3.18 (Table 8.11).

**Table 8.11. Use of e-commerce, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **2.25** | **3.44** | **4.00** | **3.31** | **2.89** | **3.18** |
| Planning and design | 3.70 | 3.83 | 4.00 | 4.43 | 4.10 | 4.01 |
| Implementation | 1.67 | 4.00 | 4.00 | 3.47 | 2.33 | 3.09 |
| Monitoring and evaluation | 1.00 | 1.50 | 4.00 | 1.00 | 2.00 | 1.90 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

A basic regulatory framework for e-commerce is in place in all EaP countries. While some countries have dedicated laws regulating practices connected to hybrid retail (Azerbaijan, Moldova, and Ukraine), relevant provisions in all of them are also covered by different legal documents. In Georgia, a new Law on E-commerce has been drafted and submitted to parliament for adoption. All frameworks include provisions for e-signatures and electronic payments, and in all countries there is an authority that monitors e-commerce platforms that process personal data, although in Azerbaijan there is no legal framework for online consumer protection. In addition, a regulatory framework on the commercial practices of paid advertisement has only been adopted in Azerbaijan, Moldova and Ukraine (Table 8.12).

## Table 8.12. Regulatory frameworks for e-commerce in EaP countries

| Country | Main legal document(s) | Consumer protection | Data protection authority | Regulatory framework on commercial practices of paid advertisement | Regulatory framework for e-signature |
|---|---|---|---|---|---|
| Armenia | Law on Electronic Documents and Electronic Signature<br>Law on the Protection of Consumer Rights<br>Law on the Protection of Personal Data<br>Law on Trade and Services<br>Government Decree No. 1976-N (defining the requirements for Internet websites, electronic applications and e-commerce platforms)<br>Central Bank Board Decisions No. 300-N and No. 2-N (on issues related to electronic payments) | Yes | Personal Data Protection Agency under the Ministry of Justice | No | Yes |
| Azerbaijan | Law on Electronic Commerce<br>Law on Electronic Signature and Electronic Documents<br>Law on Personal Data | No | Ministry of Digital Development and Transport | Yes | Yes |
| Georgia | Law on Payment Systems and Payment Services<br>Law on Protection of Consumer Rights | Yes | Personal Data Protection Service | No | Yes |
| Moldova | Law on Electronic Commerce No. 284/2004<br>Law No. 133/2011 regarding the protection of personal data<br>Law No. 114/2012 regarding payment services and electronic money<br>Law No. 91/2014 regarding electronic signatures and electronic documents<br>Law No. 105/2003 regarding consumer protection<br>Law No. 8/2016 on consumer rights when concluding contracts | Yes | National Centre for Personal Data Protection | Yes | Yes |
| Ukraine | Law of Ukraine on Electronic Commerce<br>Law on Payment Services<br>Law on Electronic Trust Services<br>Regulation on System of E-payments of National Bank of Ukraine<br>Resolution of the National Bank of Ukraine Approving Amendments to the Regulations on the Procedure for Issuing Electronic Payment Means and Carrying Out Transactions for Their Use | Yes | Ukrainian Parliament Commissioner for Human Rights (Ombudsman) | Yes | Yes |

Source: SBA Assessment questionnaire 2024.

Although these are positive steps forward, significant room for alignment with EU frameworks remains. In 2020, EU4Digital conducted a study to assess cross-border e-commerce in the EaP countries against an EU baseline, identifying key issues across the e-commerce ecosystem, the related legal frameworks and standardisation aspects (EU4Digital, 2021[18]). The assessment finds that legislative frameworks related to e-commerce platforms, parcel delivery and consumer protection need to be further strengthened (Box 8.2 provides a detailed description of the identified gaps).

### Box 8.2. Common gaps for cross-border e-commerce in EaP countries compared to the EU

**Gaps in e-commerce eco-system**

*Marketing, sales and payment*: The use of global e-commerce platforms that operate in the EU is limited because of slow/expensive delivery, preference for cash-on-delivery and poor awareness. Local EaP e-commerce platforms engaging in cross-border e-commerce are not common for the same reasons.

*Parcel delivery*: Because of the limited market size, global private operators struggle to maintain high e-commerce volumes, which results in higher rates for the consumer. Delivery times are several days slower than in the EU, where delivery within 48 hours is common.

*The EU 2021 e-commerce package*: In July 2021, the EU introduced extensive reforms to the value-added tax (VAT) and customs obligations for e-commerce to harmonise procedures related to cross-border trade. The package will include a one-stop shop for VAT, the elimination of a number of exemptions and new requirements for e-commerce platforms. Stakeholders in the EaP region remain largely unaware of the upcoming changes and there are only fragmented actions to prepare for them.

**Gaps in the relevant legal frameworks**

*Platforms*: There are only limited regulations of the terms and conditions that transparently explain the parameters determining the ranking of goods in platforms' search results.

*Parcel delivery*: Limited regulation of postal security requirements regarding the provision of electronic advance data of distance sales and insufficient preparation for the EU VAT e-commerce package limit potential cross-border trade.

*Consumer protection*: Limited regulation of misleading practices in paid advertisements, information requirements for distance contracts of digital content, and misleading omissions about consumer reviews of products reduce the transparency and reliability of local e-commerce platforms.

**Gaps in e-commerce standardisation aspects**

*Digital postal services*: Limited standardisation of electronic advanced data semantic mapping of attributes of commercial single items that are compliant with the Universal Postal Union (UPU) – World Customs Organisation rules.

*UN, EU, UPU technical standards*: Insufficient standardisation of rules regarding post, courier, express, parcel operations and customs agents that transport e-commerce items from a third country into the EU.

*The UPU technical standards*: Limited standardisation of electronic data interchange between customs authorities and postal operators on risk assessments.

*E-commerce websites' trust mark*: Lack of national e-commerce trust mark certification schemes to authenticate that a platform has made commitments to comply with the code of conduct, guaranteeing ethical standards in the digital marketplace.

Sources: EU4Digital (2021[18]), OECD (OECD, 2021[19])

In all EaP countries, governments have designed measures to promote SMEs' use of e-commerce domestically or abroad. In some cases, however, the measures have not been implemented (Armenia and Ukraine). In Armenia and Moldova, specific measures for creating a favourable environment for the development of e-commerce among SMEs are embedded in strategic policy documents (Armenia's Action Plan for the SME Development Strategy 2020-2024 and Moldova's SMEs Digital Transformation

Programme). In Ukraine, although there are no structured programmes in place, the *Diia.Business* portal offers resources (mostly guides) for businesses wishing to sell their products online.[5]

Finally, all countries except Georgia lack a monitoring mechanism to ensure that the measures implemented in support of SMEs' use of e-commerce are relevant and effective. EaP countries should also consider the introduction of e-commerce trust mark certification schemes to authenticate that a platform has made commitments to comply with the code of conduct, guaranteeing ethical standards in the digital marketplace.[6] Although none of the countries have introduced certifications, Georgia is planning to introduce similar tools. Once the new Law on E-commerce is adopted, there is a plan for sectorial association(s), under the co-ordination of MoESD and with the technical assistance of USAID, to develop a code of conduct identifying and outlining ethical standards of intermediary service providers.

### *The way forward*

- To improve export promotion among SMEs, EaP countries should strengthen the implementation of their measures by **ensuring that export promotion agencies have operational autonomy and implement their targets according to the relevant action plans**.
- All EaP countries could consider **expanding support to SMEs' integration into GVCs** by: regularly carrying out assessments of changing GVCs (Armenia, Azerbaijan, and Moldova); helping SMEs to import and establish links with MNCs; and providing incentives for FDI to further enhance MNE-SME linkages and capitalise on the resulting spill-over of technology and financial resources (see Box 8.3).
- To continue improving the support provided to facilitate SMEs' use of e-commerce, EaP countries could **introduce provisions on consumer protection and commercial practices of paid advertisement into their regulatory frameworks** and **establish e-commerce trust mark certification**.
- To continue to ease SMEs' access to trade, EaP countries could further focus on **automating and streamlining procedures and improving internal and external border agency co-operation**. In particular, they could improve the harmonisation and simplification of trade-related documents in accordance with international standards; advance in the automation of procedures; streamline procedures related to border control; and put in place or improve institutional frameworks, mechanisms and IT systems designed to improve domestic co-operation between various border agencies as well as co-operation between domestic border agencies and those of neighbouring economies and other trading partners.
- Finally, all EaP countries could consider **establishing or continue improving effective and transparent monitoring and evaluation mechanisms** to ensure that export promotion agencies and the programmes they implement across all areas covered in this dimension (export promotion, integration of SMEs into GVCs and use of e-commerce) remain efficient and effective.

### Box 8.3. Use of tax incentives to promote SME linkages in Singapore

Foreign investments in SMEs can provide access to capital, technology, and global markets, enabling them to expand their production capacity, improve product quality, and reach new customers worldwide. By fortifying the FDI-SME ecosystem, governments and policymakers can create an environment conducive to attracting and supporting foreign investments in SMEs, ultimately facilitating their integration into GVCs, which, in turn, fosters economic growth and stability. The use of tax incentives has proven effective in fostering SME linkages in various countries around the world.

In Singapore, the government has introduced Pioneer Certificate Incentive (PC) and Development and Expansion Incentive (DEI) programmes to drive innovation, attract investments, and facilitate the expansion of Singapore companies. The aim of the programmes is to encourage foreign MNEs to grow capabilities and conduct new or expanded activities in Singapore, by granting them corporate tax incentives. In particular, foreign companies are encouraged to set up in Singapore local upstream and downstream activities that are more typically conducted at companies' headquarters. Over the past decade, Singapore has awarded economic expansion-related tax incentives to approximately 600 multinational corporation (MNC) groups.

Source: (OECD, 2023[20]), (OECD, 2018[21]), (EDB Singapore, 2023[22]), (Ministry of Trade and Industry Singapore, 2021[23]).

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## Notes

[1] The International Network of Quality Infrastructure defines quality infrastructure system as "the system comprising the organizations (public and private) together with the policies, relevant legal and regulatory framework, and practices needed to support and enhance the quality, safety and environmental soundness of goods, services and processes".

[2] See: https://netzwerke.bam.de/Netzwerke/Content/DE/Standardartikel/Netzwerke/QI-FoKuS/qi-fokus-studien.html for further information.

[3] See: https://opus4.kobv.de/opus4-bam/frontdoor/index/index/docId/55498.

[4] For more information on the Enterprise Europe Network, see: https://een.ec.europa.eu/.

[5] For more information see: https://export.gov.ua/415-e-commerce.

[6] These schemes authenticate that an e-commerce company established on the national territory has made a commitment to work in compliance with the national (or regional or international) code of conduct, guaranteeing ethical standards in the digital marketplace. For more information see: https://eufordigital.eu/wp-content/uploads/2020/08/EU-eCommerce-baseline-report.pdf.

# 9 Pillar E – Innovation and Business Support

This chapter focuses on Eastern Partner countries' progress in SME innovation and business support since the 2020 assessment according to three dimensions: business development services, SME-specific innovation policy, and green economy policy for SMEs. Analysing business development services encompasses governmental provision of a wide range of support services as well as initiatives to stimulate private business support services, and the existence of such services to support SMEs' digital transformation more specifically. In addition, the dimension on SME innovation policy analyses the policy framework, and government institutional and financial support for innovative SMEs. The last dimension examines the framework for SME-specific environmental policies as well as incentives and instruments for SMEs to green their activities. Each of these three dimensions contains a dedicated set of policy recommendations for EaP countries to build on in the upcoming years.

## Introduction

Productivity growth is a key driver of economic growth and convergence. It is also the channel through which countries generate the resources needed to lift standards of living and reduce inequalities. Small and medium-sized enterprises (SMEs) are generally less productive than large companies, although the scope of the difference varies across sectors and countries. Productivity gaps between firms of different sizes are particularly evident in manufacturing, where production tends to be more capital-intensive and larger firms can exploit increasing returns to scale. A recent analysis found that labour productivity of micro, small and medium-sized enterprises in manufacturing stood at 37%, 62% and 75%, respectively, of that of large companies. Productivity gaps are less stark in the services sector, and narrowest in retail trade, which tends to display low labour productivity overall (Marchese, Giuliani and Carlos, n.d.[1]; OECD, 2021[2]).

Improved productivity is also a matter of resource efficiency. Natural resources underpin our economy by providing essential raw materials, water, and other commodities. Besides environmental benefits, their efficient use brings gains from an economic and trade perspective. A development pattern that depletes the economy's natural asset base without providing secure, long-term substitutes for the goods and services that it provides, is unlikely to be sustainable and entails risks to future growth (OECD, 2015[3]).

At the macro level, determinants of productivity include framework conditions, such as the quality of the competitive environment; the efficiency of the judiciary; financial market development; and the extent to which economic institutions facilitate access to inputs and the allocation of capital and labour to their best uses. At the firm level, drivers of productivity performance relate to managerial and workforce skills and the adoption rate of innovations. SMEs can struggle in this regard, considering that they often face difficulties in obtaining information, offering training to their employees, accessing advanced consulting services and adopting innovative processes.

This is particularly relevant when it comes to the digital transition, an area where SMEs lag behind larger firms, particularly in Eastern Partner (EaP) countries (OECD, 2021[4]). Most SMEs are not fully aware of the potential benefits in productivity and competitiveness, cannot clearly identify their needs, or do not have sufficient capabilities or financial resources to access and effectively use digital instruments. The SME digital gap compared to larger companies slows productivity growth and increases inequalities among people, firms and locations, and the COVID-19 pandemic has increased the need for businesses to operate digitally, making this issue a policy priority for governments (OECD, 2021[5]).

Innovation is also at the heart of the transition to net zero and a cleaner global environment (OECD, 2023[6]). Improved processes and new technologies can make manufacturing more sustainable, reduce pollution, increase resource efficiency, develop products and services with lower carbon footprints and yield other substantial environmental improvements.

This pillar brings together three dimensions of the assessment, which look closely at the policies in place to foster a productive, innovative and green SME sector: 1) business development services; 2) innovation policy for SMEs; and 3) green economy policy for SMEs. As presented in Table 7.1, the regional average scores for the dimensions in Pillar E do not exceed 3.5, which implies ample room for improving policy frameworks in these areas. Nevertheless, the trend observed using comparable scoring methodologies shows (moderate) progress in all dimensions since the previous SBA assessment.

### Table 9.1. Pillar E, country scores by dimension and sub-dimension, 2024

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average | *EaP average 2024 (CM)* | *EaP average 2020 (CM)* |
|---|---|---|---|---|---|---|---|---|
| **Business development services** | **3.06** | **3.33** | **4.22** | **3.69** | **3.57** | **3.57** | ***3.74*** | ***3.61*** |
| Services provided by government | 3.38 | 3.96 | 4.51 | 4.17 | 4.08 | 4.02 | *3.92* | *3.99* |
| Initiatives to stimulate private BDS | 3.14 | 3.19 | 4.10 | 3.72 | 3.20 | 3.47 | *3.57* | *3.22* |
| BDS for SME digital transformation | 3.11 | 2.91 | 3.59 | 3.51 | 3.53 | 3.33 | - | - |
| Outcome-oriented indicators | 1.40 | 1.80 | 4.20 | 1.80 | 3.00 | 2.44 | - | - |
| **Innovation policy for SMEs** | **3.00** | **2.85** | **3.44** | **3.11** | **3.03** | **3.09** | ***2.47*** | ***2.31*** |
| Policy framework for innovation | 3.06 | 3.11 | 3.50 | 2.99 | 2.72 | 3.07 | *3.06* | *2.97* |
| Government institutional support | 2.77 | 2.88 | 3.26 | 3.33 | 3.11 | 3.07 | *2.73* | *3.13* |
| Government financial support | 3.62 | 2.82 | 3.56 | 3.28 | 2.67 | 3.19 | *3.51* | *2.47* |
| Outcome-oriented indicators | 1.80 | 1.80 | 3.40 | 2.60 | 5.00 | 2.92 | - | - |
| **Green economy policies for SMEs** | **2.51** | **2.54** | **3.08** | **3.38** | **2.56** | **2.81** | ***2.99*** | ***2.59*** |
| Environmental policies | 2.89 | 2.82 | 3.57 | 3.70 | 2.44 | 3.08 | *3.16* | *3.00* |
| Incentives and instruments | 2.54 | 2.40 | 3.14 | 3.60 | 2.92 | 2.92 | *2.87* | *2.32* |
| Outcome-oriented indicators | 1.00 | 2.33 | 1.00 | 1.00 | 1.00 | 1.27 | - | - |

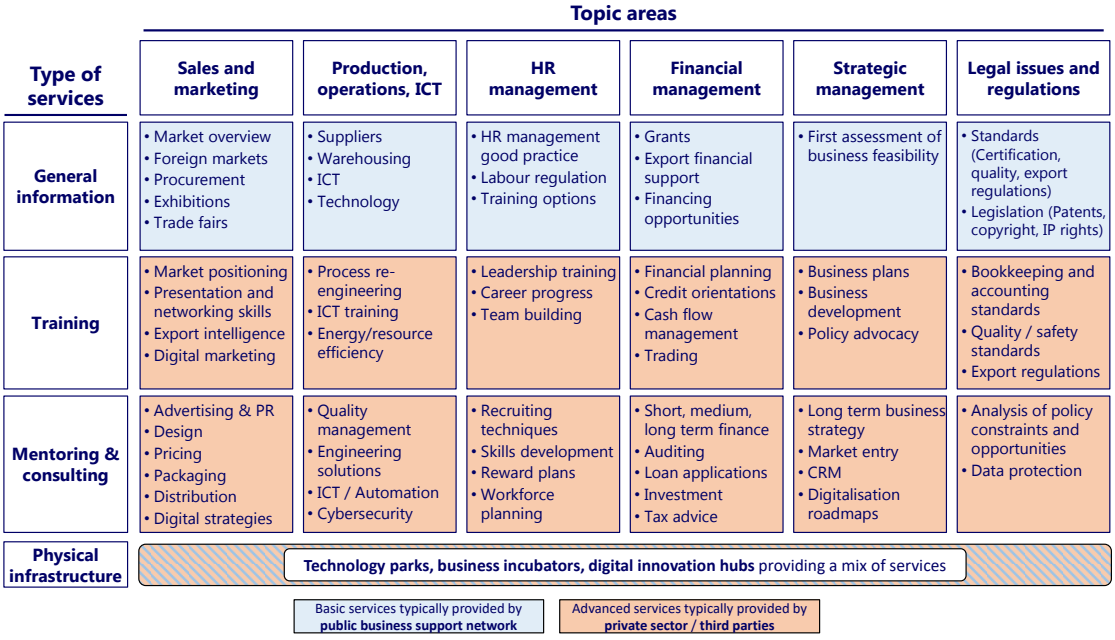
Note: BDS: business development services. CM: comparable. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Business Development Services

Business development services (BDS) enhance the performance of individual businesses, allowing them to compete more effectively, operate more efficiently and become more profitable. Such services include information provision, training, consulting and mentoring on a wide range of topics, from sales and marketing to strategic management and legal issues (Figure 9.1). BDS should also evolve to respond to changing conditions in the business environment, technological progress and market trends, as evidenced, for instance, by the current wave of initiatives to support business digitalisation, such as the European Digital Innovation Hubs (Box 9.1).

Entrepreneurs with limited skills and knowledge to start and operate a business can benefit significantly from BDS, which save time and resources, help to evaluate potential business opportunities, and encourage SMEs to enter and explore new markets. Ultimately, BDS allow firms to focus on their core competencies while outsourcing non-core tasks to specialised advisors and reducing search costs for relevant information. More advanced BDS can also provide firms with the knowledge and resources required to innovate, grow and internationalise.

## Figure 9.1. Business development services: Topic areas and types of services




Note: ICT: information and communication technologies; HR: human resources; IP: intellectual property; PR: public relations; CRM: customer relationship management.
Source: based on (OECD, 2017[7]).

BDS markets generally suffer from information-related failures regarding both the demand and supply of BDS, which disproportionately affect SMEs:

- On the demand side, SMEs often have minimal *ex ante* knowledge about the effectiveness and potential impact on firm performance, which limits their expenditure on such services. They also lack information on the availability of BDS and the type of support required, which may vary depending on the firms' type of activity and its stage of development. Finally, SMEs may simply be lacking financial resources to access BDS.
- On the supply side, BDS providers often lack adequate and up-to-date information on the SME training needs required to provide tailored and timely business support. Private BDS providers may also lack the needed skills and face uncertainty regarding compensation from SMEs and would therefore prefer working with larger companies due to more substantial contracts, longer engagement and less risky payments.

Identifying market failures – which are typically the result of information asymmetries, a lack of trust between parties and financial gaps – should be a first step in designing sound policy frameworks regarding the provision of BDS to SMEs. Governments could intervene to stimulate the emergence of vibrant markets for BDS but should avoid crowding out private initiatives. Policy interventions are then required to ensure that SMEs are informed about the benefits and availability of support services (e.g. information campaigns, awareness raising) and, if needed, incentivised (e.g. co-financing mechanisms) to increase access. Financial support should nevertheless be temporary, as such incentives, if made permanent, are vulnerable to rent-seeking. This approach would thus encourage the development of a sustainable market in BDS provision, shaped by demand, and based on a clear understanding of the company's needs and expectations.

### *Assessment framework*

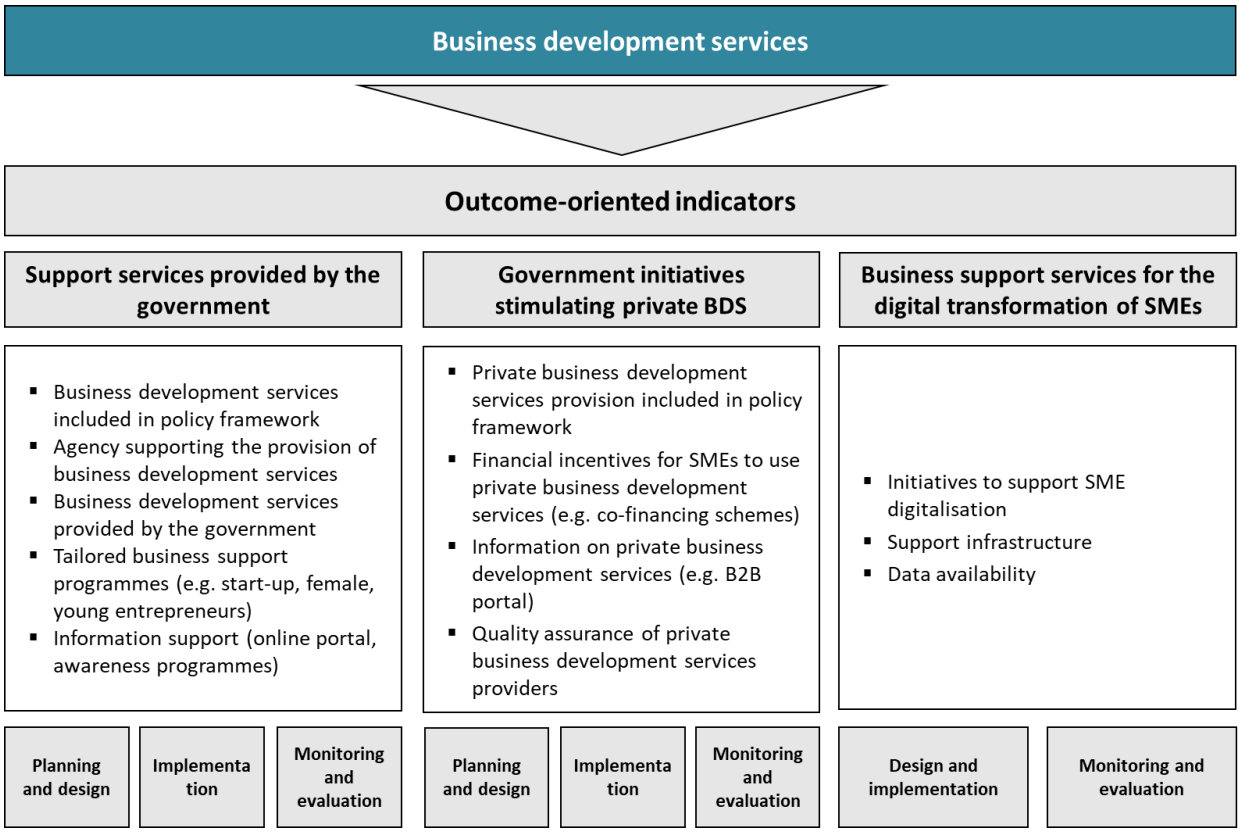
This dimension considers the availability, accessibility and effective implementation of government initiatives to design and deliver the support needed to stimulate the supply and demand for targeted BDS for SMEs. It also assesses the role of governments in identifying and addressing market failures in BDS markets through public policy tools, such as government-led business support infrastructure and initiatives to promote the development of private BDS providers.

Two important methodological changes have been introduced in this dimension since the previous SBA assessment: i) given the increasing relevance of digital technologies to support business growth and productivity, a new sub-dimension looks at the overall presence of business support services for the digital transformation of SMEs; and ii) the analysis also considers countries' ability to regularly collect quantitative information to monitor the impact of policies on actual SME performance ("outcome-oriented indicators").

As a result, the assessment framework for this dimension is composed of the following:

- **Support services provided by the government:** This sub-dimension assesses the recognition of BDS in the overall SME policy framework; the existence of a government institution with a leading role in design, delivery and monitoring of BDS for SMEs; and the extent to which public institutions provide different types of BDS tailored to the needs of different SME segments.
- **Government initiatives to stimulate private business support services:** This evaluates government initiatives aimed at stimulating private markets for BDS. This includes both demand-related factors, such as financial incentives for SMEs to purchase bespoke advisory services, and supply-related factors, such as quality assurance tools for private consultants.
- **Business Support Services for the digital transformation of SMEs:** The third sub-dimension looks at government-led initiatives to support the digital transformation of SMEs. These may include informational support, training, financial instruments and advisory services to better understand company needs, procure digital technologies and develop tailored digital road maps.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability, (typically through national statistical offices or central banks) to regularly collect statistical information about the following indicators: i) number/share of SMEs benefitting from publicly (co-)funded BDS, ii) performance of SMEs benefitting from publicly (co-)funded BDS (e.g. output growth, employment growth, export growth), and iii) a range of digitalisation-oriented indicators based on the OECD ICT Access and Use by Businesses database (i.e. number/share of businesses with a website, using social media, using enterprise resource planning software, using customer relationship management software, purchasing cloud computing services, using artificial intelligence, performing big data analytics, using the Internet of Things).

### Figure 9.2. Assessment framework – Business development services



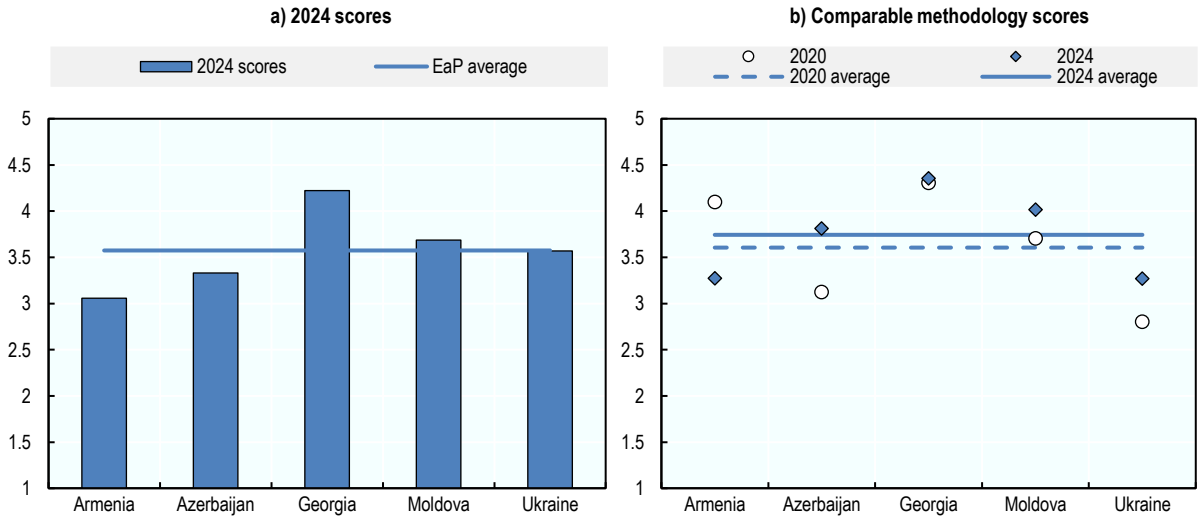

## *Analysis*

*Regional trend and comparison with 2020 assessment scores*

Average regional performance on this dimension is 3.57. While this is lower than the average score in the 2020 SBA assessment, the decrease is entirely driven by the introduction of the new sub-dimension on support services for the digital transformation of SMEs and of the outcome-oriented indicators, two areas in which countries perform worse than on the other sub-dimensions.

In fact, the in-depth assessment results for this dimension reveal a generalised improvement in countries' policy approaches to the design, implementation and monitoring of business development services for SMEs. With the exception of Armenia, all countries have strengthened their SME support agencies and have incrementally expanded the range of services targeting different segments of the SME population. This trend is reflected in the score changes between 2020 and 2024 using comparable assessment methodologies.

## Figure 9.3. Business Development Services, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/vcpftg

*Two organisational models are emerging for government agencies to manage the implementation of support services for SMEs*

The first sub-dimension assesses whether BDS are recognised in the overall SME policy framework; the institutional arrangements for design, implementation and monitoring of BDS for SMEs; and the extent to which different types of BDS are tailored to the needs of different SME segments.

## Table 9.2. Support services provided by the government, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.38** | **3.96** | **4.51** | **4.17** | **4.08** | **4.02** |
| Planning and design | 3.55 | 3.55 | 5.00 | 4.27 | 4.27 | 4.13 |
| Implementation | 3.33 | 4.39 | 4.39 | 4.28 | 4.50 | 4.18 |
| Monitoring and evaluation | 3.18 | 3.73 | 3.91 | 3.73 | 2.82 | 3.47 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Overall, EaP countries' performance in this sub-dimension has been rather stable. Although support services for SMEs have become less prominent in governments' strategic documents (e.g. national SME strategies and action plans), this has been compensated by progress in implementation and monitoring. Georgia performs the best on this sub-dimension, continuing its tradition of developing well-structured SME strategies and action plans, relying on two strong implementing agencies. It is also the only country in the region with an advanced system to evaluate the impact of its support programmes on SME performance (See Box 12.3 in the Georgia chapter).

Two models are emerging for SME agencies to manage the implementation of support services for SMEs, which can be interpreted as the strategic choice of governments seeking to maximise their assistance to

the SME population, given i) the size of their countries and ii) the extent to which the ecosystem of support service providers can complement government initiatives.

- Smaller countries with a relatively limited community of support service providers, such as Georgia and Moldova, choose to have a strong role in the direct management and delivery of support programmes. Their national SME agencies, ODA and Enterprise Georgia and ODA (Organisation for the Development of Entrepreneurship), offer a wide range of support mechanisms (financial and non-financial) and engage in a continuous update of their services to meet evolving SME needs. From the point of view of the SME manager or individual entrepreneur, they are the go-to institutions helping SMEs and in most cases are the direct providers of support services.
- Larger countries with a vibrant community of non-governmental service providers, such as Ukraine, opt for a more decentralised approach, acting as a platform and leveraging the capabilities of other actors in the ecosystem (e.g. international donors, local authorities, business associations). The online portal *Diia.Business*, managed by the Entrepreneurship and Export Promotion Office (EEPO), is without doubt the most developed and information-rich one-stop shop for SMEs in the EaP region, representing a gateway for Ukrainian entrepreneurs into the universe of support services available in the country, searchable by geographic location and type of support (e.g. financing, training, consultations).

Regardless of the model chosen, this assessment round reveals a trend towards strengthening SME support agencies across the EaP region. In Moldova, ODA (previously ODIMM) has undergone a reorganisation to incorporate stronger governance mechanisms (clearer mandate, qualification requirements for top management, audited financial statements); in Azerbaijan, KOBIA has expanded its activities and improved its monitoring mechanisms; and in Ukraine, EEPO is now a full-fledged SME support agency, with a broader mandate, more stable financial resources, and more numerous and qualified staff than the previous SME support unit advising the Ministry of Economy. The only exception to this trend is Armenia, where the capacity of the government to assist the SME population has been reduced due to the closure of the previous SME agency, SME DNC, and the transfer of its functions to other government entities.

In addition, since the last SBA assessment, several SME agencies have expanded their geographical footprint and opened offices outside the capital cities in an attempt to better serve local SMEs. This is the case for Azerbaijan (3 SME houses and 21 SME Development Centres), Ukraine (14 *Diia.Business* Support Centres), and Georgia (3 regional growth hubs). This physical expansion can take place either by opening tenders for independent actors willing to operate local offices of the national SME agency in a “franchise” model (Ukraine) or by keeping all operations, and related costs, internal to the agency (Georgia).

Finally, the range of available support services provided by the government is evolving, demonstrating an improved understanding of the needs of SMEs in the EaP region. While most countries have established financial support instruments for start-ups and trainings on basic business skills, some (Georgia and Moldova, especially) are introducing more complex programmes for different categories of SMEs and their specific needs, such as on greening production, digitalisation, internationalisation and technology upgrades.

### *Role and involvement of private BDS providers is (slowly) increasing*

This sub-dimension measures government mechanisms to promote the development of private markets for BDS provision and stimulate the use of private BDS by SMEs.

### Table 9.3. Government initiatives to stimulate private BDS, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | *EaP average* |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.14** | **3.19** | **4.10** | **3.72** | **3.20** | ***3.47*** |
| Planning and design | 3.00 | 2.60 | 3.93 | 4.20 | 3.33 | *3.41* |
| Implementation | 3.31 | 3.44 | 4.33 | 3.67 | 3.49 | *3.65* |
| Monitoring and evaluation | 3.00 | 3.67 | 3.89 | 3.00 | 2.33 | *3.18* |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

EaP countries' average performance on this sub-dimension has improved slightly, with the most significant progress occurring in Azerbaijan and Moldova. Moldova, in particular, is the only EaP country acknowledging the role external consultants play in its national SME strategy and action plan, which explains its high score in the planning and design thematic block for this sub-dimension. Across the region, however, governments' involvement of private players in the provision of BDS to SMEs remains limited or, at least, below potential.

First, governments can directly outsource some of their services for SMEs, especially trainings and consultancy, to specialised advisors. This is the most common form of involvement of private BDS providers across the EaP region, with all countries making use of this option in at least some respect. The clearest example is Azerbaijan, where SMEs can easily request consulting support from advisors pre-selected by KOBIA. Typically, these services are free of charge for end users, and while this format may ease access to business advice for financially constrained entrepreneurs, it also risks distorting the market by over-subsidising services that SMEs might otherwise be willing to pay for.

Second, governments can subsidise (a share of) the costs of consulting services incurred by SMEs through dedicated voucher schemes or other co-financing mechanisms. In practice, a more common version of this kind of support adopted by EaP countries' SME agencies is to include expenses on business advisors among the eligible costs of broader grant programmes for start-ups and SMEs, as is the case in Georgia and Moldova. This approach has several advantages, as i) it allows SMEs to obtain advisory services from external consultants of their choice as opposed to pre-selected experts; ii) it makes specific industry or business expertise more affordable to SMEs, while typically requiring a cost-sharing mechanism from beneficiaries; and iii) it helps SMEs understand the value they can get from external advisors, thus stimulating demand and, in turn, the supply of consulting services in the countries.

Finally, governments can help increase SME awareness of external advisors by providing information on the availability and quality of private consultants. This can be done, for instance, through publicly available databases of providers of business development services and digital marketplaces, complemented by some quality assurance mechanisms. In the EaP region, only Moldova's SME agency (ODA) offers this type of information, with a dedicated section of its website listing dozens of private consulting firms, their contact details, a short description of their areas of expertise, as well as the possibility for SMEs to rate their experience working with them.

An important initiative that should be mentioned in this area is the EBRD's "Advice for Small Business" programme. The programme complements governments' efforts to enable SMEs to access local consulting services by working on both sides of the market: on the demand side, the programme provides SMEs with co-financing to cover part of the cost of the advisory project (usually in the range of 50-60% of the total cost); on the supply side, it delivers business training and capacity building to local consultants to increase their expertise and ability to serve SMEs. According to the EBRD's own data, the programme delivers important results for participating SMEs in EaP countries: 60% of them experience significant job creation and 83% see 28% increase in turnover , on average, within one year of advisory project completion (EBRD, 2021[8]).

*Tailored programmes to support the digital transformation of SMEs have started to appear*

This new sub-dimension captures the availability of dedicated government-led initiatives to support the digital transformation of SMEs, looking at both financial and non-financial instruments.

**Table 9.4. Business support services for the digital transformation of SMEs, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.11** | **2.91** | **3.59** | **3.51** | **3.53** | **3.33** |
| Design and implementation | 3.22 | 3.04 | 3.51 | 3.47 | 3.51 | 3.35 |
| Monitoring and evaluation | 2.85 | 2.60 | 3.76 | 3.60 | 3.58 | 3.28 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

The digitalisation of government services for businesses has been many years in the making, across OECD and non-OECD countries. In particular, a large number of dedicated online platforms have been set up to help SMEs and entrepreneurs liaise with the public administration and cut red tape. Typically, these "single digital portals" or "digital one-stop shops" serve as single entry points for accessing digital government services and reducing redundancy in requests from the public administration (OECD, forthcoming[9]). The digitalisation of businesses, primarily intended as the adoption of digital technologies, has also become a very visible trend since at least the early 2000s. The COVID pandemic, however, provided a short-term boost in this direction, requiring many SMEs to move online for the first time to be able to continue their operations.

All EaP countries recognise the importance of supporting SMEs' digital transformation, although the extent to which this becomes an explicit policy priority translating into concrete support varies greatly across the region. Trainings on various digitalisation-related topics (e.g. transferring business processes online, digital marketing, digital finance) are the most common form of support provided by national SME agencies in EaP countries. Such trainings are typically free of charge, often delivered online, and represent an important first step in the range of services that governments can offer to SME managers and their employees willing to build their skill sets for the digital economy. The "one-to-many" nature of these trainings, however, cannot address the specificities of individual SMEs, which require tailored analysis and recommendations developed by specialised consultants.

For these reasons, some countries have also started to introduce full-fledged programmes for SME digitalisation, delivering individualised assessments and company-specific digitalisation road maps for beneficiaries, complemented by dedicated financial support instruments to procure digital technologies or obtain further specialised advisory services. Moldova has been the "first mover" in this area, with ODA's dedicated initiative for SME digitalisation operational since 2022, which also included, in its first version, a digital maturity self-assessment. Georgia has followed suit: in 2023, Enterprise Georgia introduced a new programme as part of its regional growth hubs' services to help SMEs improve their digital skills and adopt digital technologies. With the assistance of digital transformation experts, SMEs first undertake an overall business diagnostic exercise and then develop a tailored plan with recommendations on how to digitalise their operations. Co-financing mechanisms to purchase digital solutions and develop digital skills are also available in both countries, up to EUR ~9 000 in Georgia and EUR ~26 000 in Moldova. In addition, the EU-funded EU4Digital facility opened its EU4Digital Academy, providing free-of-charge digital skills training to SMEs' employees in EaP countries, in areas such as digitalisation of businesses, digital marketing and e-commerce (EU4Digital, 2023[10]).

The potential contribution of non-governmental actors to further SME digital transformation should also be noted. Countries where SME agencies have not (yet) introduced advanced support instruments in this area should consider the pool of active players in the ecosystem as potential partners in the development of

new support programmes for SME digitalisation. This is especially the case for Armenia and Ukraine, where donor-led initiatives, such as EBRD-trained consultants on SME digitalisation (Armenia) or the fast-growing IT sector (Ukraine) could supply the industry expertise and act as mentors for traditional SMEs to advance in their digital transformation.

Finally, EaP countries' practices to build the evidence base on the state of SME digitalisation shows ample room for improvement. Only Georgia and, to a lesser extent, Ukraine regularly collect statistical indicators on businesses' adoption of digital technologies with data broken down by enterprise size class; and Armenia carried out a first pilot survey in 2023 following Eurostat's model on ICT Usage in Enterprises. These are important indicators to monitor in order to determine whether smaller companies can bridge the digitalisation gap with larger ones, which has been highlighted as a determinant of productivity inequality among firms (OECD, 2021[4]).

### Box 9.1. European Digital Innovation Hubs

European Digital Innovation Hubs (EDIHs) help companies as well as public sector organisations to respond digital challenges and become more competitive. Through their regional presence, they can easily reach local companies and address them in the local language while also giving them access to the broader innovation ecosystem. As the network of digital innovation hubs is EU-wide, companies can benefit from European best practices across hubs, which foster co-operation and knowledge transfer between all stakeholders. This unique combination of regional expertise, paired with a European network, enables well-tailored support on digital transformation with access to a community of hubs.

**Digital Innovation Hub services**

EDIHs receive 50% of their funding from the European Commission and 50% from the respective member state, associated country, or region, or from private sources. The hubs' services can be divided into four main categories: i) access to technical expertise and the opportunity to "test before invest" in new technology, often through the involvement of third-party companies; ii) support to identify financing and investment opportunities; iii) provision of trainings and skill development; and iv) access to the innovation ecosystem and European network to share skills, resources, and knowledge.

EDIHs have proven to be important enablers for the digital transformation of SMEs. This best practice can be replicated under the EU's Economic and Investment Plan for the EaP region, which is worth EUR 2.3 billion in grants, blending and guarantees, with a potential to mobilise up to EUR 17 billion in public and private investments (EIB, 2020[11]).

**Latvia's Digital Innovation Hub**

Latvia's Digital Innovation Hub mainly targets SMEs and is co-ordinated by the local IT Cluster. It aims at supporting the digital transformation of local companies by i) raising awareness about the benefits of digitalisation through marketing campaigns, "kickstart" workshops, networking events and trainings on general digital skills; ii) matchmaking with mentors and providing small grants (EUR <5 000) to test new technologies; iii) providing support for technology adoption, through grants and other financial instruments for process digitalisation as well as dedicated skill upgrades; and iv) fostering further digital transformation via corporate hackathons, access to industry experts and grants for more innovative technologies.

Source: (European Commission, n.d.[12]); (Latvia's Digital Innovation Hub, n.d.[13]).

### *The way forward*

As EaP countries update their policy approaches to design and implement business development services for their SME populations, the following recommendations could be taken into consideration.

- All EaP countries can benefit from **the inclusion of dedicated measures to deliver BDS for SMEs in strategic policy documents**, which can provide certainty and medium-term planning in implementation. This is particularly relevant for Azerbaijan and Ukraine, which at the moment lack dedicated national strategies for SME policy, although SMEs appear as an important target of Ukraine's National Recovery Plan drafted in 2022.
- As countries expand the local presence of their SME support agencies, they should devise ways to **ensure the sustainability of regional offices** through strong quality-control mechanisms (if

outsourced, such as in Ukraine) and cost/benefit analysis (if developed internally, such as in Azerbaijan and Georgia).

- To leverage the existence non-governmental business development services, **EaP countries could embed single information portals with information on all actors in the BDS ecosystem into their SME agencies' websites**, including donor-led initiatives and private quality-assured consultants. Ukraine's *Diia.Business* portal (https://business.diia.gov.ua/en/business-map) offers a useful example in this respect and an opportunity for peer learning within the EaP region.
- To **develop a more market-based provision of BDS to SMEs**, EaP governments could consider outsourcing support services to private BDS providers and increasing the offer of co-financing mechanisms to SMEs for first-time BDS use, enabling firms to choose their preferred providers. This could be particularly useful in countries such as Azerbaijan, where many BDS are provided free of charge and where such financial support instruments are missing.
- Facing evolving SME needs, EaP countries (especially Armenia, Azerbaijan and Ukraine) could upgrade existing initiatives and **develop dedicated support programmes for SME digitalisation**, which should include elements to enhance digital skills, company-specific digitalisation road-maps and financial support tools to facilitate technology adoption. In addition, further investment in cyber-security (skills and technologies) are needed in all EaP countries, as a key enabler to increase trust and the uptake of digital solutions.
- While there has been good progress across the region in monitoring the implementation of action plans and programme take-up, **there is a need to improve the evaluation of business support programmes, in particular to assess the impact of BDS on various measures of SME performance**, as well as on the emergence of the overall BDS market**.** Georgia's experience could be a useful example in this respect (See Box 12.3 in the Georgia chapter).
- To build the evidence base to monitor SME digitalisation, all EaP countries could expand the collection of statistical indicators on the adoption of digital technologies in the business sector. The OECD database on ICT Access and Use by Businesses offers an important methodological reference in this respect.

## Innovation policy for SMEs

The OECD/Eurostat Oslo Manual (4th edition) defines business innovation as "a new or improved product or business process (or combination thereof) that differs significantly from the firm's previous products or business processes, and that has been introduced on the market or brought into use by the firm" (OECD/Eurostat, 2018[14]). It distinguishes between three types of innovation based on their degree of novelty: an innovation can be new to the firm, the market or the world. By introducing new knowledge and technologies in the firm's production process, innovative practices and activities help firms expand and boost productivity, even if only a small percentage of them advance to the global technological frontier (EBRD, 2014[15]).

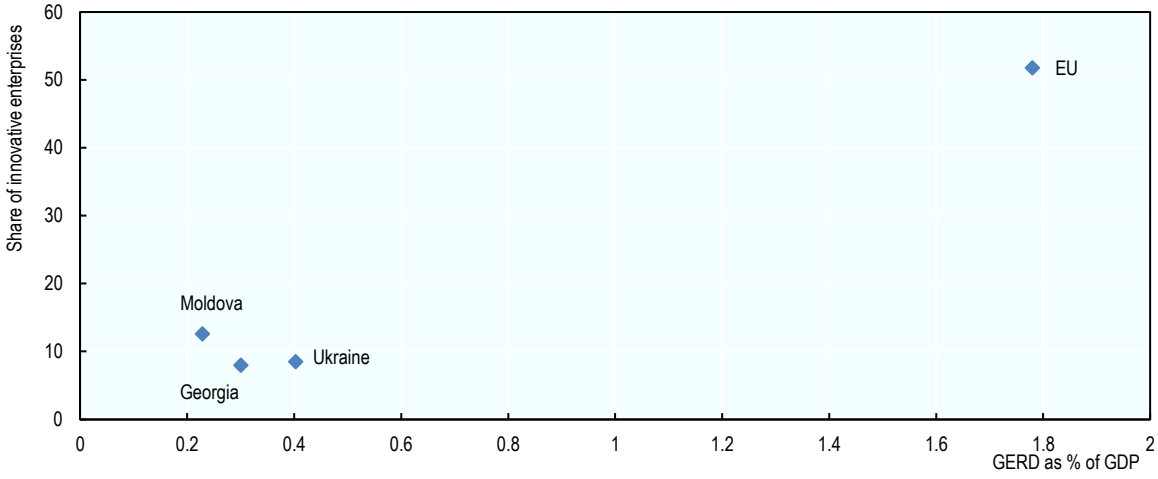
Beyond increasing economic output, recent developments and global trends have demonstrated the role innovation can play in tackling global social and economic challenges. Innovation and research and development (R&D) have been at the forefront of the global response to the outbreak of COVID-19, including through the development of vaccines and medical treatments, but also by providing digital solutions to tackle social distancing, which has accelerated the automation and adoption of digital technologies in many spheres of society, and has often been driven by the private sector (OECD, 2022[16]).

SMEs are essential for the generation and diffusion of innovations, but face difficulties in developing and scaling up innovative activities due to their limited size and financial and staff capacity. Although some SMEs are innovation leaders in their field, they generally tend to introduce fewer new products and technologies than larger, more established firms.

Governments can support innovation through public investment in science and R&D. Specifically for SMEs, policy makers can also foster innovation at the firm level, by building an ecosystem conducive to co-operation among firms and creating linkages with universities and research centres, encouraging the use of applied research outputs, facilitating access to technology, protecting intellectual property, and introducing financial incentives for firms to engage in innovative activities.

While a data breakdown on innovation activities in the business sector by enterprise size class is not available, overall innovation performance in the EaP region remains well below that of EU countries (Figure 9.4), both in terms of innovation inputs (gross domestic expenditure on R&D, or GERD, as % of GDP) and innovation outputs (share of enterprises introducing product or process innovation).

### Figure 9.4. Innovation performance in EaP countries vs. EU (2020)




Notes: GERD = gross domestic expenditure on research and development. Data for innovative enterprises in Georgia (process innovation) are for 2022. Data for Armenia and Azerbaijan are not available.
Source: National Statistical Offices for EaP countries; Eurostat for the EU.

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### *Assessment framework*

This dimension considers the strength of the policy framework for innovation, with particular reference to SME innovation, the different support services provided by governments to stimulate innovative activities by SMEs, and the availability of direct and indirect financial support instruments to incentivise SME innovation.

Compared to the previous SBA assessment, the main methodological changes introduced in this dimension are the removal of a sub-dimension on “non-technological innovation” (while keeping relevant questions and incorporating them into the other sub-dimensions) and the analysis of countries’ ability to regularly collect quantitative information to monitor the impact of policies on actual SME innovation performance (“outcome-oriented indicators”).

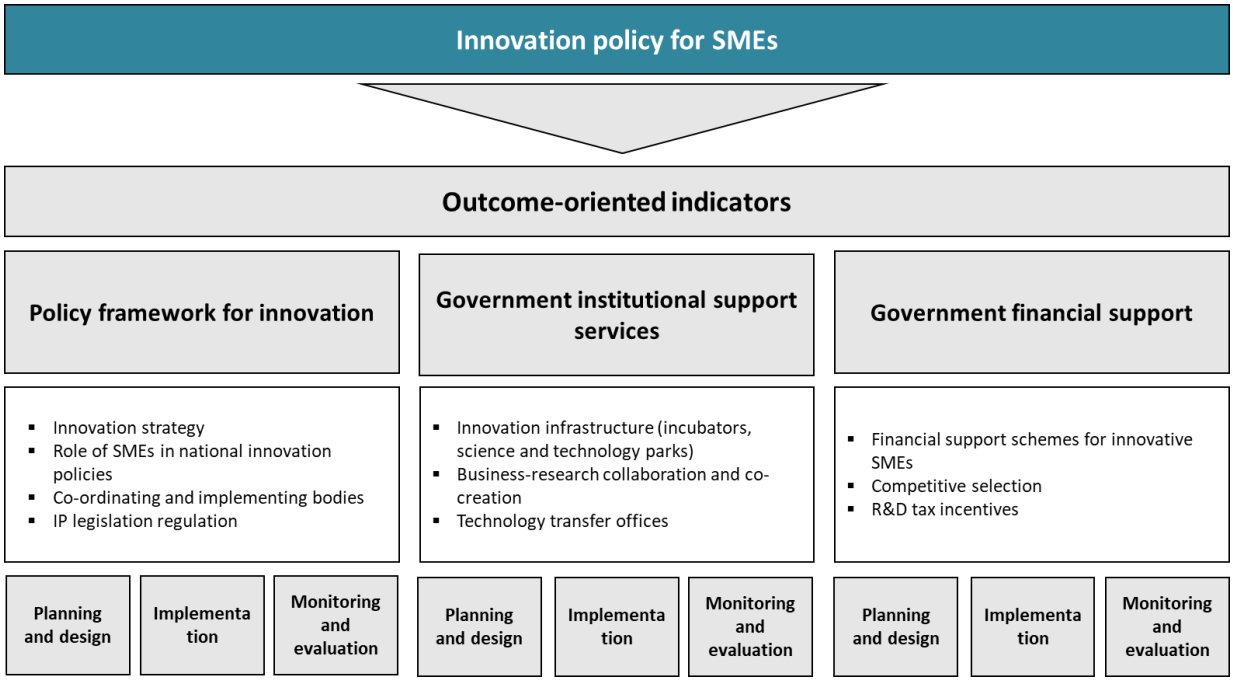
As a result, the assessment framework for this dimension is composed of the following:

- **Policy framework for SME innovation:** This sub-dimension assesses the overall policy approach to foster innovation in the business sector, with particular reference to dedicated national strategic frameworks, the existence of a co-ordinating agency and specific provisions for SMEs.
- **Government institutional support services for innovative SMEs:** This captures the availability and quality of institutional measures to support innovation in the SME sector, with a focus on

innovation infrastructure: incubators, science and technology parks, innovation centres and technology transfer offices.

- **Government financial support for innovative SMEs:** Here, the availability of direct and indirect financial support measures to encourage SMEs to innovate and carry out R&D activities is evaluated. The role of demand-side policies such as public procurement of innovation and functional procurement is also considered.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability, (typically through national statistical offices or central banks) to regularly collect statistical information about the following indicators: i) labour productivity in SMEs; ii) SMEs introducing product/process innovations; iii) R&D expenditure in the business sector, by business size class; and iv) sales of new-to-firm innovations as a share of the firm's turnover.

### Figure 9.5. Assessment framework – Innovation policy for SMEs



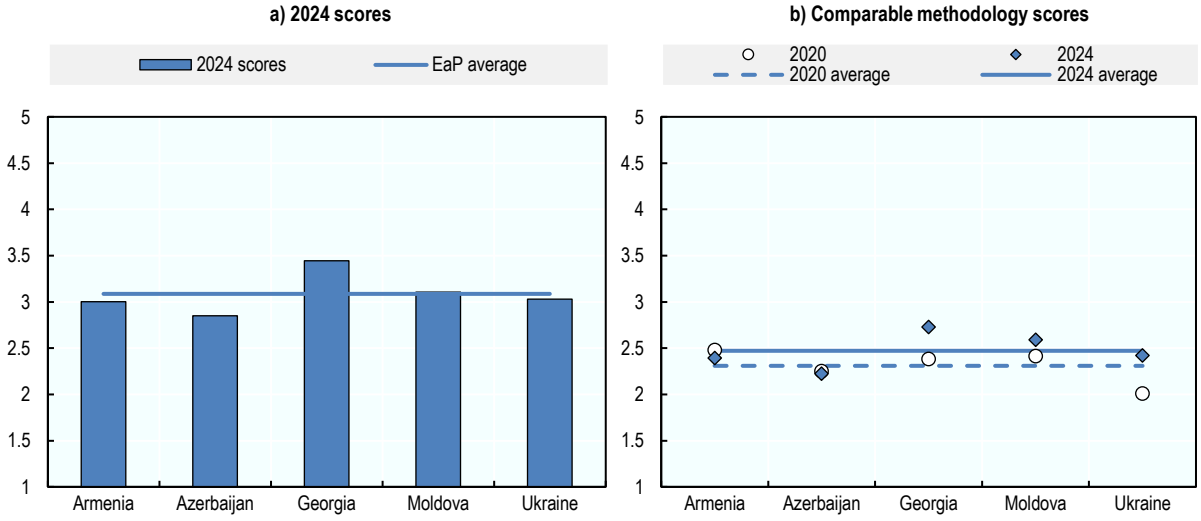

## *Analysis*

*Regional trend and comparison with 2020 assessment scores*

Regional performance on this dimension is reflected in an average score of 3.09. This is a slight increase compared to the 2020 SBA assessment, and is also reflected in the regional trend visible using comparable assessment methodologies.

While the policy frameworks for innovation have not evolved greatly in the last four years, the options for obtaining financial support for innovative SMEs have become more diversified and represent the area with the most interesting developments. The main improvements are recorded in Ukraine, which started from the lowest base in 2020 and whose performance is also boosted by the national statistical office's advanced practices to collect outcome-oriented indicators for this dimension.

## Figure 9.6. Innovation policy for SMEs, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### *Policy frameworks for innovation lack a strong focus on SME innovation*

This first sub-dimension looks at the overall strategic approach that SME policies are based on, as well as co-ordination and implementation mechanisms. It evaluates the level of development of the overarching policy framework for supporting the innovation of the business sector, especially of SMEs.

## Table 9.5. Policy framework for innovation, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **3.06** | **3.11** | **3.50** | **2.99** | **2.72** | **3.07** |
| Planning and design | 3.56 | 3.03 | 3.08 | 3.13 | 3.40 | 3.24 |
| Implementation | 3.27 | 3.58 | 3.93 | 3.04 | 2.47 | 3.26 |
| Monitoring and evaluation | 1.70 | 2.20 | 3.25 | 2.60 | 2.10 | 2.37 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Policy frameworks for innovation in EaP countries have not substantially improved since the previous SBA assessment. Dedicated national strategies for innovation with clearly defined and operational action plans tend to be the exception rather than the rule, and only present in Moldova (the "National Programme in the Field of Research and Innovation 2020-2023") and Ukraine (the "Innovation Development Strategy 2030"). However, countries compensate for this shortcoming by incorporating elements of innovation policy in other strategic documents, such as the governments' broad strategy for socio-economic development (Armenia and Azerbaijan) and/or the national SME strategies (Armenia and Georgia). Nevertheless, innovation and SME industrial or technology policy remain generally separated. This, in turn, continues to hamper science-business linkages for intellectual property, and prevents the integration of innovation angles into large-scale SME support programs that effectively deliver on established performance goals. Additionally, specific policy targets on SME innovation remain very rare, which can be interpreted as a

reflection of the limited understanding of the barriers to SME innovation and relatively low ranking of this policy area in EaP governments' economic reform priorities.

On the institutional setting and implementation side, countries' performance is more heterogeneous. Traditionally, support for innovation in EaP countries has been directed to universities and research centres carrying out fundamental research, often administered by the responsible ministries. However, in the last decade, EaP governments have re-oriented the focus of their support for innovation towards the business sector. As a result, dedicated innovation agencies have been created in some EaP countries (Georgia, Moldova and, most recently, Azerbaijan), but their mandates and areas of intervention differ greatly and range from start-up development to technology transfer and go as far as carrying out nuclear research (Azerbaijan). Georgia's Innovation and Technology Agency appears to be the best example in the region, with a track record of providing a wide range of support instruments for start-up development and the IT sector.

Monitoring and evaluation of innovation policies for SMEs show ample room for improvement. Three main factors appear to be behind the relatively low performance in this area. First, as national policy documents do not focus on the SME sector, there is a scarcity of SME-specific initiatives that can be assessed. Second, EaP countries typically tend to monitor the implementation of activities rather than evaluate the impact of support programmes; the only exception in this regard is Georgia, which is planning to expand Enterprise Georgia's impact evaluation methodology to Georgia's Innovation and Technology Agency's (GITA) operations as well. Third, outcome-oriented indicators in the area of SME innovation are generally not available, with the notable exceptions of Azerbaijan and Ukraine. Ukraine participated in the EU Community Innovation Survey 2020 and reports on nationwide statistical information on sales of new-to-firm innovations as a share of turnover. Azerbaijan's statistical office compiles data on R&D expenditure by enterprise size class.

*Institutional support is slowly evolving, with interesting developments in technology transfer*

The second sub-dimension assesses the availability of institutional support for innovative SMEs, including innovation infrastructure such as incubators, science and technology parks, technology transfer offices and innovation centres.

### Table 9.6. Government institutional support services for SMEs, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension score** | **2.77** | **2.88** | **3.26** | **3.33** | **3.11** | **3.07** |
| Planning and design | 3.00 | 3.00 | 3.70 | 3.70 | 3.30 | 3.34 |
| Implementation | 3.08 | 3.17 | 3.33 | 3.33 | 3.00 | 3.18 |
| Monitoring and evaluation | 1.67 | 2.00 | 2.33 | 2.67 | 3.00 | 2.33 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

Government in-kind support services for innovative companies continue to expand in EaP countries, although they remain heavily oriented towards assisting entrepreneurs active in the digital and IT sectors. All countries have more or less widespread networks of incubators and accelerators supporting business creation and innovative start-ups with co-working facilities, trainings and networking opportunities. Such initiatives can be managed directly by governments (Azerbaijan's SABAH.lab) but are often sponsored and implemented by private players (Ukraine Start-up Fund's accredited accelerators), non-governmental organisations (Moldova's Tekwill) and the donor community (Armenia's Enterprise Incubator Foundation).

Science and technology parks can also support resident companies (both newly created and established ones) with logistical infrastructure as well as research and prototyping laboratories. Progress in this area

has been more mixed: Georgia's GITA has expanded its physical infrastructure and opened two new techno parks (now eight in total); Armenia, Azerbaijan and Moldova have not introduced considerable expansions to their existing facilities; Ukraine adopted several laws to stimulate the development of industrial parks and manufacturing in the country, and even though 60 industrial parks were registered as of early 2023, most of them are reportedly not active and the government did not allocate any budget in this area in 2022.

The most interesting developments have occurred in the area of science-business linkages, where EaP countries' performance has traditionally been very weak in spite of a legacy of directing public funding towards supporting basic research carried out by public universities and research organisations. This has started to change in recent years, with renewed efforts to promote science-industry interactions, technology transfer and co-creation of knowledge. This is particularly the case in Georgia, where the innovation agency, GITA, carried out a first technology transfer pilot programme with the goal of identifying scientific outputs with high commercial potential and assisting the research teams to negotiate licensing and business deals with potential business partners. Ukraine has also expanded its network of Technology and Innovation Support Centres (17 active in 2023), offering support to innovators to register for IP protection, enter into IP agreements with partners and clients, and help with technology search.

### *Government financial support for innovative SMEs remains primarily focused on the IT sector*

This sub-dimension analyses the availability and effectiveness of the direct and indirect financial incentives the EaP governments are providing to encourage SMEs to engage innovative activities, from investing in R&D to purchasing innovative technologies.

**Table 9.7. Government financial support for innovative SMEs, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **3.62** | **2.82** | **3.56** | **3.28** | **2.67** | **3.19** |
| Planning and design | 3.55 | 3.00 | 3.55 | 3.55 | 3.18 | 3.36 |
| Implementation | 3.86 | 3.00 | 3.86 | 3.29 | 2.71 | 3.34 |
| Monitoring and evaluation | 3.22 | 2.11 | 2.91 | 2.78 | 1.67 | 2.54 |

Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

The lack of financing is reportedly one of the most important constraints on innovative activities, given the inherently risky nature of innovation and uncertainty of financial returns. The problem is even more pronounced for smaller, knowledge-intensive companies due to the relative intangible nature of their assets. Governments can help overcome such obstacles by making it easier for SMEs to innovate and reduce the financial risk of investing in innovative projects. Well-designed financial support aims at catalysing experimentation with new ideas, "crowding-in" private investment in R&D and acknowledges the complexity of engaging in innovation activities and accompanying SMEs along the entire innovation cycle (development, engineering, production and commercialisation).

Overall, the average performance of EaP countries on this sub-dimension has improved since the previous SBA assessment, mostly driven by positive developments in Armenia and Ukraine. However, a disproportionate focus on the IT sector and start-up segment persists. While this can be seen as a response to the growing IT skills and IT-oriented entrepreneurship in the EaP region[1], governments should not neglect other sectors that could benefit from public support to innovation. Agriculture, for instance, could benefit from the diffusion of relatively simple technologies to increase the productivity of what still remain mostly small-scale producers.

Direct financial support instruments for innovative SMEs have become available in all EaP countries. These typically take the form of grants in the range of USD 9 000 (Ukraine) to EUR 54 000 (Georgia) and can have diverse objectives, such as to stimulate enterprise creation and idea commercialisation (Armenia and Ukraine), facilitate prototyping and improve manufacturing (Moldova), and develop products and services with the potential for internationalisation (Georgia). Such grants are typically awarded via a competitive process and, even though they can make a real difference for the winners, they are, by design, only able to reach a limited number of beneficiaries. Furthermore, the extent to which risk-sharing features are considered when designing grants for innovation varies greatly from country to country: while Azerbaijan's grants do not require any contributions from beneficiary SMEs, Moldova's "Program to Support Digital Innovations and Technological Start-ups" covers at most 80% of the amount of the investment project, and Georgia's innovation matching grants (discontinued in 2022) required up to 50% of the eligible project costs to be secured from beneficiaries. It should also be noted here that EaP countries continue to be eligible for the main EU funding programme for research and innovation (Horizon 2020, followed by Horizon Europe), although their actual participation in terms of funding received, especially by SMEs, is very small (Box 9.2).

Indirect financial incentives for innovation and R&D remain rare and limited with respect to the targeted sectors and business population. Azerbaijan has introduced a "Startup certificate", through which micro and small businesses can benefit from a tax exemption on the profits generated by the sale of innovative products or services for a period of three years. The Ukrainian government has recently established *Diia.City*, a legal and tax environment incentivising investment and employment for companies operating in the IT sector. The most interesting development in this area has occurred in Armenia, which has introduced a new set of "measures to modernise the economy". Through this programme, entrepreneurs benefit from subsidised loan and leasing agreements to purchase new machinery and equipment. This package has been very well received by Armenian entrepreneurs, with nearly 1 000 credit and leasing agreements signed in the first 9 months of the programme and manufacturing companies reportedly starting to export thanks to the increased quality of their production.

### Box 9.2. EU support for research and innovation: Horizon 2020 and Horizon Europe

Following Horizon 2020, the biggest EU research and innovation programme with a budget of almost EUR 80 billion of funding, an even bigger successor programme called Horizon Europe was launched in 2021 with a budget of EUR 95.5 billion until 2027. The new programme is meant to facilitate collaboration and strengthen the impact of research and innovation within the context of economic development. The investments made possible through the programme should boost economic growth and enhance industrial competitiveness.

Horizon Europe consists of three pillars, reflecting the topics of excellent science, global challenges and European industrial competitiveness, and an innovative Europe, which are built upon the evaluation of the previous Horizon 2020 programme. The first pillar is promoting financing for researchers through the European Research Council and provides fellowships to new talented researchers. The second pillar is exploiting European clusters supporting collaborative research on key subjects such as health and digitalisation. The third pillar includes the new feature of the European Innovation Council that especially focuses on supporting SMEs and start-ups. The new programme is supposed to maximise the impact of the investments in research and innovation through better access to support also for riskier investments and more collaboration on a European level.

EaP countries participate in Horizon Europe and participated in Horizon 2020 with different degrees of involvement. Georgia and Ukraine have benefitted the most, with the highest amounts of contributions received and the largest degree of SME participation. Ukraine and Armenia were awarded the largest average grant.

#### Table 9.8. Participation of EaP countries in Horizon 2020 and Horizon Europe

| Country | Net EU contribution (EUR) | Participating entities (number of unique organisations) | Average grant (EUR) | SME share of EU contribution | Number of unique SMEs involved in projects |
|---|---|---|---|---|---|
| Armenia | 7 163 926 | 23 | 159 198 | 2.3% | 4 |
| Azerbaijan | 686 989 | 19 | 28 625 | 0.0% | 0 |
| Georgia | 11 141 839 | 44 | 148 558 | 4.8% | 3 |
| Moldova | 10 478 020 | 48 | 105 839 | 17.9% | 7 |
| Ukraine | 63 195 461 | 210 | 208 566 | 31.0% | 47 |

Note: Numbers in the table refer to EaP countries' participation in both Horizon 2020 and Horizon Europe as of July 2023. OECD analysis on selected indicators since the beginning of Horizon 2020. Armenia, Georgia, Moldova and Ukraine are "associated countries" and as such enjoy equal participation rights as EU member states.
Source: (European Commission, 2023[17]).
Source: Horizon Europe (europa.eu) How Horizon Europe was developed (europa.eu).

### Box 9.3. Indirect financial incentives for innovation

Governments can support innovation in the business sector through both direct and indirect financial incentives. On the one hand, direct incentives such as grants and subsidised loans are a common way to encourage SMEs to innovate. These direct financial supports are, however, prone to misallocations as they are received by the beneficiaries before any investment is made.

On the other hand, indirect incentives provide a good alternative as they are granted after the firm has already invested in new technology or R&D activities. Examples of indirect support are broad-based (i.e. available to a large number of companies) fiscal incentives, such as tax allowances, exemptions or deductions, as well as tax credits. The specific functioning of the tax benefit, however, differs depending on the instrument: while tax allowances, exemptions and deductions reduce the taxable amount before assessing the tax, a tax credit is the amount subtracted directly from the beneficiary's tax liability after it has been computed. With regard to R&D, allowing related expenses to be fully deducted remains the default among OECD countries.

Indirect financial incentives need to also be carefully designed in order to be beneficial for the addressed firms. Tax benefits on profit, for example, might not lead to the desired stimulation of investment in innovation among SMEs, particularly in the case of innovative start-ups, which may not yet make any profits and thus may not be able to take advantage of such tax benefits. Thus, for firms with insufficient tax liability, standard types of tax relief instruments do not work efficiently on their own. Indirect support instruments can, therefore, be refined further to address these segments of companies.

One way to do so is through carry-over provisions of tax benefits. These are popular instruments among OECD countries and partner economies, as they allow moving the tax benefit on profits to future years. Thus, when the company will make a profit, it will be able to claim the carry-over and reduce its tax payment for that period. The time horizon for the claim can be finite or infinite, and varies substantially across OECD countries: in 2022, it ranged from 3 years (the Czech Republic) to 20 years (the United States).

A step further is the provision of offsetting payments or "refunds", which can be particularly beneficial for young and innovative firms at the stage of investing in developing and launching their products. In this case, the tax authority uses a tax refund to cover the company's unpaid claims and thus setting these off with their tax credit. This can also be applied to offset payroll taxes or social security contributions.

Source: (OECD, 2021[18])

### *The way forward*

While renewing their policies to build a more innovative SME sector, EaP countries should focus on the following reform priorities. The EC-OECD STIP Compass database (https://stip.oecd.org/stip/) collects information on innovation policies across OECD and partner countries and could inspire policy reforms in the EaP region based on international policy examples.

- All EaP governments can better **highlight the role of SME innovation in their strategic documents**. Whether in national strategies for innovation or in sectoral SME strategies, the specific obstacles for SME innovation should be acknowledged, addressed through dedicated measures and monitored against SME-specific policy targets.

- Some countries (especially Armenia and Ukraine) could **strengthen their co-ordination and implementation capacity** by clearly identifying bodies tasked with supporting SME innovation and building staff capacity to design and implement dedicated programmes.
- To foster science-business linkages, governments should **build the skills of agencies tasked with technology transfer** and **intensify co-operation between academia and the private sector**. This is particularly relevant for countries where successful donor-led initiatives are coming to an end (e.g. Georgia) or where governments' efforts are at a very initial stage (e.g. Armenia). For instance, enhancing co-operation would require promoting start-ups based on applied research insights and co-financing of research services, as well as ensuring closer ties between applied public research and its commercial demand and potential applications.
- When devising specific support programmes for SME innovation, governments should **consider assisting the SME population beyond the start-up segment** as well as services to support technology absorption in more mature SMEs (as is the case in Georgia and Moldova).
- With regards to direct financial incentives for innovation, governments (especially Azerbaijan and Ukraine) should **ensure that a matching component is required when awarding grants/soft loans**, to share risks with beneficiaries of financial instruments for innovation.
- Governments should also **consider introducing more flexible indirect financial incentives for innovation,** which are more market-based and less prone to distortions than direct instruments (Box 9.3), and **broadening the set of potential beneficiaries of support programmes**. Alternative finance, crowdfunding, and cooperation with networks of business angels can be considered.
- Last, to empower national administrations to monitor and evaluate the impact of their innovation policies, governments should **strengthen the national statistical office's capacity to collect information about SME innovation performance**. Eurostat's Community Innovation Survey and the European Innovation Scoreboard offer useful references in this respect.

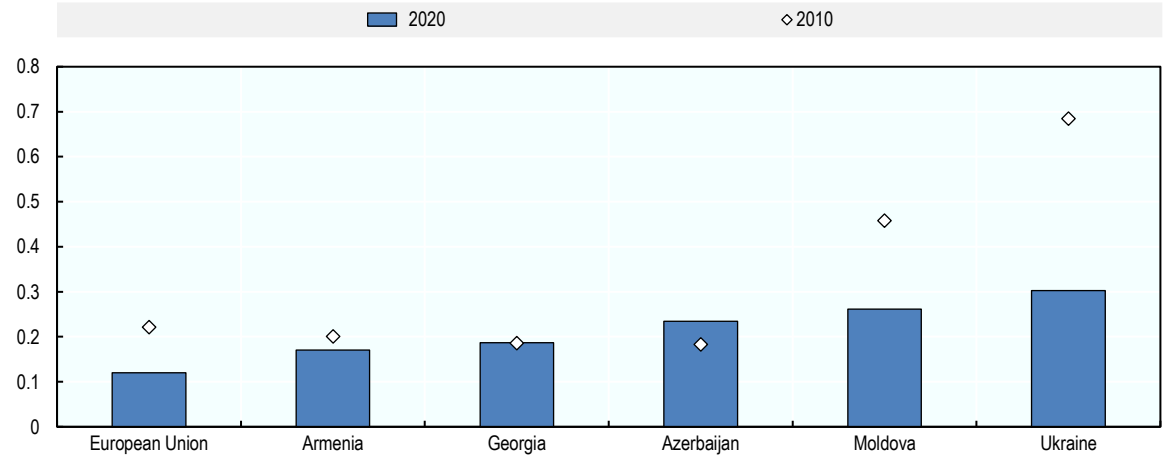
## SMEs in a green economy

Human-induced climate change is under way and accelerating, leading to many weather and climate extremes in every region across the globe. This has led to widespread adverse impacts, disrupting economies, transforming eco-systems, and causing damages to nature and people, especially the most vulnerable groups (IPCC, 2023[19]). To address this key global policy challenge, countries are pledging to mitigate and adapt to climate impacts with self-defined Nationally Determined Contributions, detailing their commitments to cut greenhouse gas emissions and limit global average temperature rise to 1.5°C above pre-industrial levels.

The primary focus has traditionally been on large corporations, seen as the largest emitters of greenhouse gases. However, it is estimated that over 80% of their emissions are derived from their supply chains, which are often composed of smaller enterprises that perform essential services in the production process. Thus, although individual SMEs may not be large carbon emitters, the collective emissions of this business segment, amounting to roughly 90% of businesses worldwide, mean that SMEs will be critical to achieving global decarbonisation targets (WTO, 2022[20]). EaP countries have ample margins to decarbonise their economies to bring them closer to greener economies (Figure 9.7).

## Figure 9.7. Carbon intensity of EaP economies

CO2 emissions per unit of GDP (kg per PPP USD of GDP)




Note: PPP = purchasing power parity.
Source: World Bank, World Development Indicators

StatLink https://stat.link/k1a60i

Environmental challenges, and related "green economy" opportunities, deserve further attention from policy makers when it comes to the promotion of biodiversity and combating environmental degradation. Biodiversity and eco-system services provide invaluable – but often invisible – benefits at global, regional and local scales. These include services such as nutrient cycling, habitat provisioning, pollination, erosion control and climate regulation. The need to mainstream biodiversity and ecosystem services more effectively into national and sectoral policies has recently gained renewed impetus on the global policy agenda (OECD, 2018[21]).

Furthermore, a growing number of companies worldwide recognise the advantages of resource efficiency and cleaner production in terms of reduced costs in materials, energy, water and compliance with environmental requirements, as well as in responding to customers', investors' and local communities' expectations. However, SMEs, and particularly micro-businesses, have limited capacity to learn about and interpret environmental regulations, along with financial constraints to invest in green practices beyond environmental requirements (OECD, 2023[22]).

Governments have a range of tools at their disposal to support SMEs in adopting greener practices. These can be roughly divided into regulatory, financial, and informational tools. Regulatory tools involve using the regulatory system to incentivise better environmental performance, including by providing incentives for firms that exceed environmental standards. Financial tools include ensuring that SMEs can access financial resources to implement green practices, as well as helping to create markets, for example by implementing green public procurement policies. Informational tools include providing SMEs with the information they need to adopt green practices, as well as providing recognition and certification for those that do. Good policies can help shift the conversation about greening SMEs into a discussion about the business benefits that greening can bring, rather than the costs.

A key issue for SMEs is understanding the benefits of adopting more resource-efficient practices, and the positive impact that these practices can have on their bottom line. While businesses may be aware that they can reduce their costs by using less energy, water and material inputs and by cutting their waste levels, they may not be aware of how to do it, or whether they are able to fund it (OECD, 2018[23]) Addressing this issue includes supporting access to finance, as well as providing direct support to SMEs

in terms of what measures they can take to improve their performance. Governments also have a role in improving the business case for SMEs, by developing new markets through green public procurement, and by recognising green achievement through awards and ecolabels and communicating it to the public (OECD, 2018[23]).

### *Assessment framework*

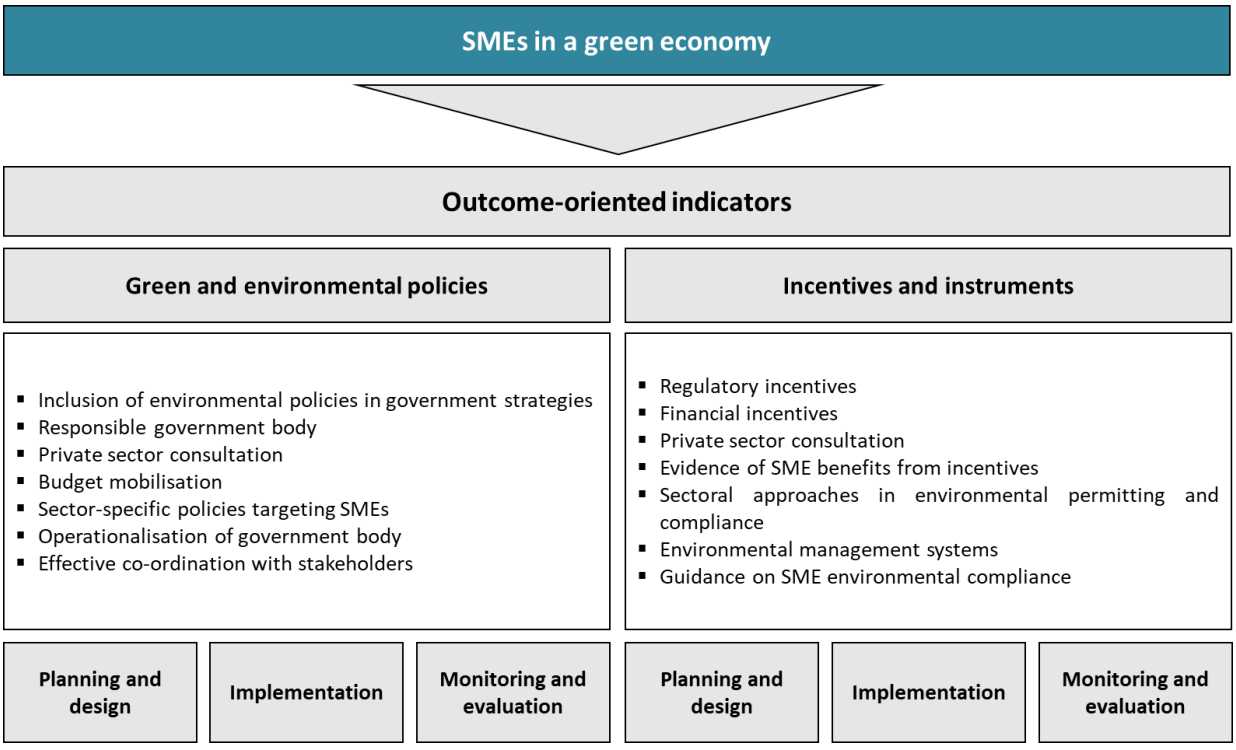
This dimension analyses governments' approaches to help SMEs improve their environmental performance, both via the general policy framework for green and environmental policies, as well as through dedicated regulatory and financial incentives.

Small changes have been introduced to the methodology of this dimension since the previous assessment: to better capture reporting requirements on environmental performance and the availability of green finance instruments; and to analyse countries' ability to regularly collect quantitative information about actual SME environmental performance ("outcome-oriented indicators").

As a result, the assessment framework for this dimension is composed of the following:

- **Framework for green and environmental policies targeting SMEs:** This sub-dimension examines the overall set of environmental policies targeting SMEs, as well as the greening aspects in national SME, sectoral and innovation policy frameworks. It also considers the presence of operational government agencies assisting SMEs with the adoption of greener practices.
- **Incentives and instruments:** The second sub-dimension explores the existence and implementation of different instruments and measures of whether the government provides regulatory and financial incentives to SMEs, whether there is any evidence that SMEs benefit from those incentives, and how such support schemes are structured and delivered.
- The section on **outcome-oriented indicators** for this dimension considers countries' ability, (typically through national statistical offices or responsible government agencies) to regularly collect statistical information about the following indicators: SMEs having adopted environmental management systems; SMEs having implemented resource-efficiency and pollution-reduction measures; SMEs that offer green products or services; SMEs with a turnover share more than 50% generated by green products or services; and the number of environmental public procurement contracts.

### Figure 9.8. Assessment framework – SMEs in a green economy



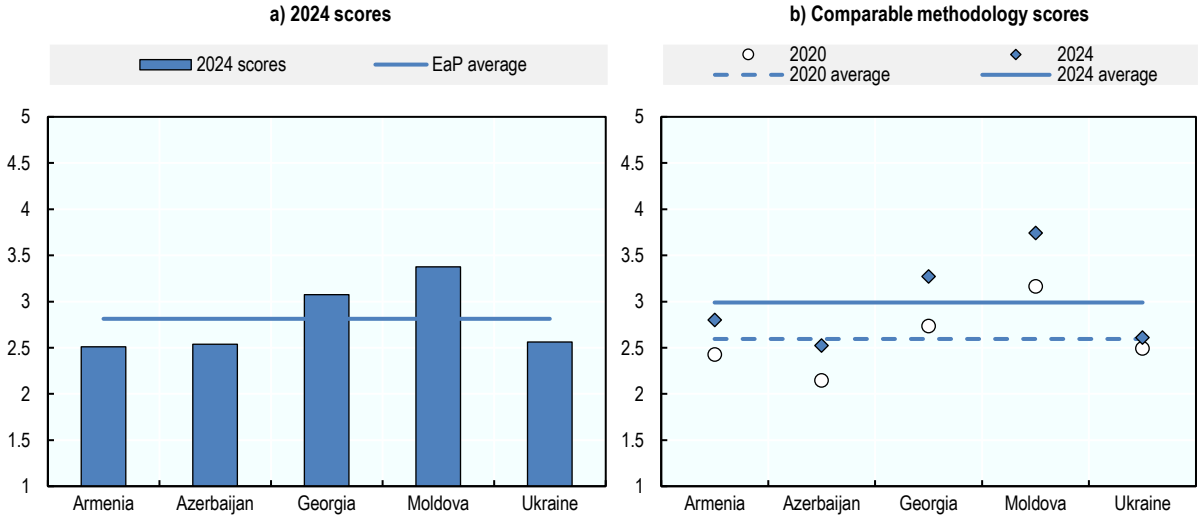

## *Analysis*

### *Regional trend and comparison with 2020 assessment scores*

Regional performance on this dimension is reflected in an average score of 2.81. This is a marginal improvement compared to the 2020 SBA assessment, although it becomes more pronounced when looking at scores generated by comparable assessment methodologies.

Overall, policy settings for environmental protection across the region rarely address SME specificities, and financial incentives are not widely available. Moldova is a welcome exception in this respect; it is both the best performer and the country that has improved the most on this dimension, thanks to the clear recognition of SMEs in recently adopted environmental policies, as well as to the introduction of dedicated financial support instruments for SME greening.

## Figure 9.9. SMEs in a green economy, dimension scores




Note: See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### *Environmental policy frameworks rarely address SME specificities*

This first sub-dimension evaluates the introduction of greening initiatives in the policy framework for SMEs. It examines whether strategic enterprise and innovation policy documents cover eco-efficiency and eco-innovation, and the extent to which SMEs are explicitly reflected as a target group.

## Table 9.9. Policy frameworks for greening SMEs, sub-dimension scores

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **2.89** | **2.82** | **3.57** | **3.70** | **2.44** | **3.08** |
| Planning and design | 3.00 | 3.00 | 4.32 | 3.40 | 3.62 | 3.47 |
| Implementation | 3.00 | 3.16 | 3.16 | 4.00 | 1.83 | 3.03 |
| Monitoring and evaluation | 2.45 | 1.73 | 3.18 | 3.55 | 1.73 | 2.53 |

Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

This round of SBA assessment reveals how all EaP countries acknowledge the importance of supporting green economic growth in high-level planning documents, a sign that environmental concerns are becoming more salient as governments in the region join the global trend to mitigate the causes and adapt to the effects of climate change. However, the focus on SMEs in such strategic documents remains rather limited. Only Georgia, Moldova and, to a lesser extent, Armenia include specific provisions for SMEs in their strategic policy documents. Moldova's national development strategy "European Moldova 2030", clearly stipulates greening SMEs as a priority through the creation of green jobs and the promotion of eco-innovations and eco-labelling for products and services offered by SMEs. Georgia included the "Development of the Green Economy for SMEs" as one of the seven strategic directions of its ongoing SME Development Strategy 2021-2025, with specific actions to develop eco-tourism, eco-innovation and access to green finance. Other EaP countries lag behind in this respect, with no clear mention of SME-related initiatives or measurable targets in their strategic policy documents. While it may be worth noting

that some of the countries (Azerbaijan) have adopted green economy policies that will affect SMEs, they do not specifically target this segment of the enterprise population and therefore risk overlooking their specific size-related barriers and needs to improve SME environmental performance.

On the implementation side, SME agencies in the EaP region typically do not engage in the promotion of greening initiatives, and the ministries responsible for environmental issues tend to minimise outreach to SMEs. As a result, SME considerations in overall guidance and support on environmental policy for businesses remain limited, and often left to sectoral business associations. The only exception in this regard is Moldova, where ODA, the local SME agency, has assumed a strong role in promoting greening practices directly to entrepreneurs (see the next section). Furthermore, most countries have not committed significant budgets to supporting the greening of SMEs, and many programmes and initiatives remain heavily reliant on donor funding.

Finally, monitoring and evaluation persists as the weakest area of this sub-dimension for almost all the countries. The generalised lack of SME-specific activities and targets in environmental policy documents means that governments do not commit to look at the effects of their policies on the SME sector, and even when there are SME-specific policy actions (such as in Georgia and Moldova), the focus is on monitoring implementation rather than on impact evaluation. This is also because all countries have very limited statistical production of outcome-oriented environmental indicators, which is a prerequisite to track progress of SME environmental performance at the national level.

### *Incentives and instruments for green SMEs remain rare, but all countries have made some progress*

The second sub-dimension considers the various tools and instruments in place to support SMEs in their greening efforts. It particularly explores whether governments provide regulatory and financial incentives to SMEs, whether there is any evidence that SMEs benefit from those incentives, and how such support schemes are structured and delivered.

**Table 9.10. Incentives and instruments, sub-dimension scores**

| | Armenia | Azerbaijan | Georgia | Moldova | Ukraine | EaP average |
|---|---|---|---|---|---|---|
| **Sub-dimension scores** | **2.54** | **2.40** | **3.14** | **3.60** | **2.92** | **2.92** |
| Planning and design | 3.61 | 2.39 | 3.50 | 4.39 | 3.55 | 3.49 |
| Implementation | 2.39 | 2.58 | 3.36 | 2.82 | 2.85 | 2.80 |
| Monitoring and evaluation | 1.00 | 2.00 | 2.00 | 4.00 | 2.00 | 2.20 |

Note: See the “Policy framework, structure of the report and assessment process” chapter and Annex A for information on the assessment methodology.

Traditionally an area of weak performance due to the regulatory focus on large polluters and a generalised lack of SME-specific financial incentives, this sub-dimension records some progress for all countries since the previous SBA assessment, although the reasons for this trend vary.

Environmental regulation represents one of the most effective ways by which governments can directly influence the environmental performance of SMEs. Environmental regulatory reforms are being introduced in the region, mainly through risk-based environmental assessment/permitting and to disincentivise environmentally harmful practices. As an example, Armenia has shifted to a risk-based approach for its environmental impact assessments of economic activities, with different procedures depending on the severity of possible environmental hazard. In Azerbaijan, in accordance with the Law "On the Rational Use of Energy Resources and Energy Efficiency" approved in 2021, several Decisions of the Cabinet of Ministers were subsequently approved and are expected to stimulate enterprises to implement energy efficiency measures. In parallel, Georgia has developed a set of General Binding Rules (GBRs) for the

poultry sector aimed at reducing the environmental impact of SMEs without putting an undue burden on their operations. Moldova, on the other hand, continues to use deterrents to reduce the use of natural resources and limit pollution, in particular through established tax measures for the use of natural resources (e.g. water, minerals, timber) and charges for environmental pollution.

Environmental management systems (EMSs) can also promote green behaviour by allowing an enterprise to be recognised for setting environmental objectives and consistently controlling its operations in order to achieve them. Most EaP countries (Armenia, Azerbaijan and Ukraine) are promoting the adoption of EMSs, through information campaigns, but lack dedicated financial support for SMEs. This may slow down uptake, as SMEs face size-related human and financial resource constraints to adopt and get certified for EMS-related standards.

The use of information instruments is increasing. Azerbaijan has developed a new online self-assessment tool for greening SMEs to help them assess their environmental performance[2] (EU4Environment, 2021[24]). Moldova also launched a self-assessment tool for entrepreneurs, a platform that shows SMEs how to improve resource efficiency and environmental performance, increasing their competitiveness by reducing their costs[3]. By completing the online questionnaire, businesses receive customised recommendations based on the characteristics of their enterprise. By mid-2023, some 1200 Moldovan enterprises had benefitted from this digital tool. (EU4Environment, 2020[25])

Thanks to EU-funded support, capacity building among SMEs in EaP countries has promoted awareness of circular economy benefits. Training for increasing resource efficiency and tailored expert assessments and advice have helped pilot enterprises to achieve significant savings of raw materials, water, and energy. Clubs of green-minded SMEs (Box 9.4) have been established in several municipalities across the region, with specific business cases developed based on the achievements of the enterprises participating in these pilot initiatives. However, while clear progress has been made, the scale of action is still modest.

### Box 9.4. Local knowledge networks for applying Resource Efficient and Cleaner Production

Production with fewer resources, less pollution, and better productivity is at the core of Resource Efficient and Cleaner Production (RECP). The RECP methodology has proven to be effective in allowing SMEs to lower production costs while improving their competitive advantage and the impact on the environment. In EaP countries, its application has been supported by the EU with UNIDO's technical involvement. Established to speed up the uptake of resource efficient practices by SMEs, the so-called RECP Clubs are based on a scalable model for rolling-out RECP in groups of enterprises. The enterprises adopt a coaching and guidance programme designed to help them improve performance by undergoing a self-assessment.

UNIDO has monitored the achievements of RECP Club members. For example, during 2015-16, over 250 enterprises were members of 22 RECP Clubs throughout all EaP countries. During the training modules, expert visits and counselling sessions offered within the RECP Clubs, the participating companies learned to develop action plans for RECP (with some already implementing the improvement measures within their production). The identified measures allowed the industries to make annual savings on energy (24,884 MWh), materials (61 thousand tonnes) and water consumption (1.3 MM of m³), while reducing production costs (EUR 4.2 million) and CO2-eq emissions (41,255 tonnes) cumulatively. Support for RECP Clubs is ongoing and will continue.

Source: (EU4Environment, 2023[26])

Dedicated financial incentives for greening SMEs are rare across the EaP region. Moldova has advanced the most, with the introduction in 2020 of two new SME support programmes implemented by the local

SME agency ODA (the “Greening Programme for SMEs” and the “Energy Efficiency Programme for SMEs”). These represent a good practice in the region, as SMEs can benefit from information materials, consultancy support, and training services to identify solutions and take concrete actions to green their production processes, complemented by grants up EUR 75 000 for investment in machinery and equipment using alternative energy sources. In the period November 2020 – August 2022, 85 companies from diverse sectors benefited from such grants (Government of Moldova, 2022[27]).

Governments’ efforts in this area in other EaP countries lag behind, although some incentive schemes exist for companies to adopt greener practices (not specifically for SMEs), for instance to transfer to green electricity consumption and generation (Armenia and Georgia). In many cases, donor-funded initiatives play an important role in filling the financing gap for green-oriented investment, such as the EU-financed “Promoting Green Lending in the Eastern Partnership” project, which channels green financing to SME through local commercial banks and the EBRD-led “Finance and Technology Transfer Centre for Climate Change” (FINTECC) initiative, including its EU4Climate window, which helps businesses adopt climate technologies for renewable energy and resource efficiency.

An interesting development is the introduction of the Sustainable Finance Taxonomy in 2022 by the National Bank of Georgia, which provides a classification system for identifying activities that deliver on climate, green, social or sustainability objectives and is expected to create a framework for green companies to be easily identifiable and have easier access to concessional loans financed by green funds and development banks. In a similar vein, Azerbaijan’s Entrepreneurship Development Fund started considering ESG criteria in the financing decisions of its concessional loans. With EU support, work on analysing the potential of capital markets has been carried out in EaP countries with a focus on green bonds and their potential to raise additional resources for the transition to a green, low-carbon and resilient economy (EU4Environment, 2023[28]).

Lastly, public procurement can also offer opportunities and incentives for companies to adopt greener practices. “Green” public procurement is either planned or already operational in a number of countries (Georgia, Moldova and Ukraine), but implementation levels and accessibility for SMEs remain hard to determine. Ukraine, in particular, introduced the notion of "life cycle cost" into the Law on Public Procurement, which allows contracting entities to consider the environmental impact of the procured goods or services among the tender assessment criteria.

### Box 9.5. Fiscal incentives for adopting environmentally friendly technology in the Netherlands

Environmental Investment Deduction (MIA) and Arbitrary Depreciation of Environmental Investments (Vamil) are two separate tax schemes designed to promote Dutch companies' investments in environment-friendly technology.

Introduced in 2000, MIA is a fiscal instrument through which Dutch companies can deduct 27% to 45% of the costs of an environmentally friendly investment, in addition to their regular investment tax deductions. The percentage that can be deducted from taxable profit are explicitly determined in an "Environment List" ; the benefits thus depend not only on the applied tax scheme (corporate or income tax), but also on the investment itself. This scheme ultimately reduces profit tax. MIA's budget for 2023 is EUR 192 million.

In parallel, Vamil was introduced in 1991. Through this tax measure, Dutch entrepreneurs can determine themselves when to write off 75% of their investment costs. This scheme accelerates depreciation and thus gives businesses an immediate tax benefit equivalent to approximately 4-5% of the total investment. The Vamil budget for 2023 is EUR 25 million.

The Vamil scheme is often applied together with MIA – i.e. an application for MIA often qualifies a company for Vamil. Hence, the combination of these two environmental subsidies allows a business to maximise the advantage on a single, environment-friendly, investment. Such fiscal incentives are particularly beneficial and thus attractive for SMEs: they are the most represented firm group in submitted applications, despite both schemes being accessible to businesses of all sizes.

Source: (OECD, 2018[23]).

### *The way forward*

To advance their policy frameworks to support greener SMEs, EaP governments could consider the following reform priorities:

- Government should **align SME support policies with national decarbonization and green economy policies and targets.** SME greening should be mainstreamed across broader SME policy documents, such as national strategies for SME development or innovation, to ensure that SME economic development goes hand-in-hand with improved environmental performance. This should be done with due attention to the specific needs and capacities within the SME sector. At the same time, environmental and climate regulations should be adapted to reflect the particularities of this segment of enterprises.
- To increase awareness and help SMEs go green, governments should **strengthen their institutional capacity to provide guidance to SMEs**, for instance by including this as part of the SME agencies' mandate. The use of digital tools could magnify the outreach of awareness and capacity building efforts.
- In doing so, the **business case for improving environmental performance should be emphasised**, and government agencies could leverage a diversity of intermediaries (sectoral business associations, local governments, financial service providers) to enhance outreach to SMEs. A simplified environmental management system for SMEs could be proposed, as it allows them to progressively advance their environmental performance.
- As SMEs adopt innovative tools to improve their environmental performance, it will be important to **facilitate partnerships and best practice sharing among businesses** to support SME greening activities (e.g. resource efficiency, circular economy).

- Governments should also ensure that **public procurement policies adopt green/sustainable assessment criteria** in their tenders, so as to create a demand for greener products, services and production processes. In addition, public procurement officials will have to ensure that green procurement opportunities are known and accessible to SMEs. These policies should also enhance innovation by linking payments to performance criteria and allowing bidders to find innovative ways to meet such requirements. This approach would optimise the chances of finding practices that are both more environment-friendly and more efficient financially – which, when found, will be decisive and catalytic for SME greening.
- SMEs in EaP countries would also benefit from **increased availability of financing instruments for investing in greener equipment and processes**. This could be done through tax incentives for greener businesses (see Box 9.5), as well as by developing specific financing mechanisms targeting SMEs (e.g. grants, soft loans). In parallel, commercial banks' capacity to report on sustainable financing should be increased to reward ESG-oriented lending.
- Lastly, governments could **improve the statistical production of environmental indicators**, which are a prerequisite for strengthening tools to evaluate the impact of SME greening policies, certification and support programmes on actual SME environmental performance.

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## Notes

[1] In 2020, the EU4Digital facility developed recommendations to improve access to finance for SMEs specialised in digital innovation in Georgia and Ukraine, focusing on three sources of financing: alternative finance, crowdfunding, business angels. The assessments provide a comparison of the gaps in both countries in these sectors, with tailor-made recommendations in line with European best practice (EU4Digital, 2020[29]).

[2] https://yb.smb.gov.az/form

[3] https://eco.odimm.md/form

# Part II. Country profiles

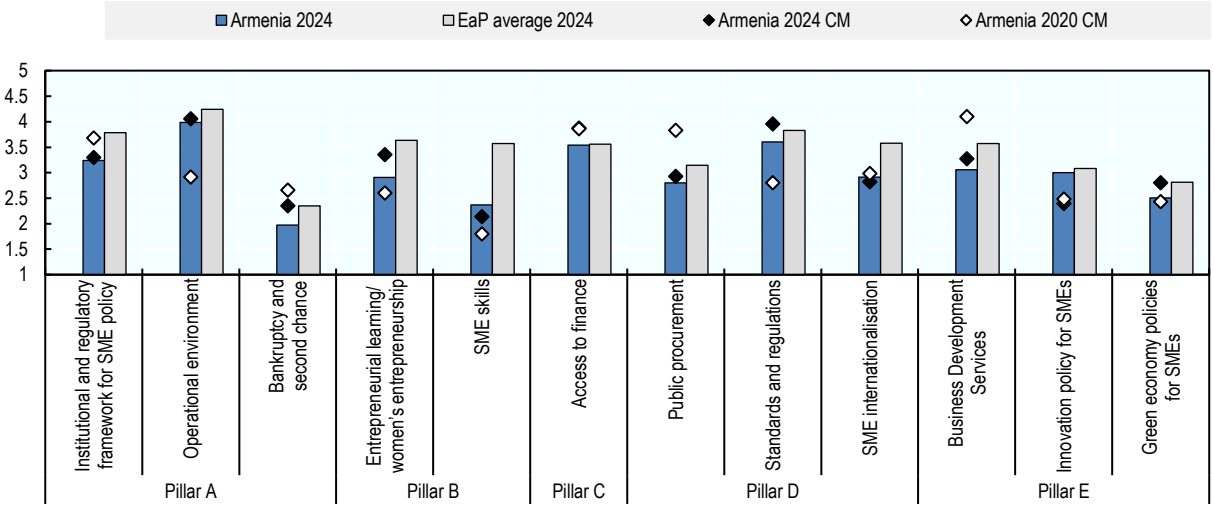
# 10 Armenia: Small Business Act country profile

This chapter provides an assessment of the progress made by Armenia in implementing the Small Business Act (SBA) for Europe over the period 2020-23. It starts with an overview of Armenia's economic context and dives further into the characteristics of the country's SME sector. It then develops on the state of selected framework conditions for the digital transformation of SMEs. Finally, it analyses Armenia's progress along twelve measurable dimensions grouped in five thematic pillars and sets out targeted policy recommendations.

## Key findings

### Figure 10.1. SME Policy Index scores for Armenia

Country scores by dimension, 2024 and 2020 vs 2024 CM




Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### Table 10.1. SME Policy Index scores for Armenia

Country scores by dimension, 2024 and 2020 vs 2024 CM

| Pillar | Dimension | Armenia 2024 | EaP average 2024 | *Armenia 2024 (CM)* | *Armenia 2020 (CM)* |
|---|---|---|---|---|---|
| Pillar A | Institutional and regulatory framework for SME policy | 3.24 | 3.78 | 3.29 | 3.68 |
| | Operational environment | 3.99 | 4.24 | 4.05 | 2.92 |
| | Bankruptcy and second chance | 1.97 | 2.35 | 2.35 | 2.66 |
| Pillar B | Entrepreneurial learning/ women's entrepreneurship | 2.91 | 3.64 | 3.35 | 2.60 |
| | SME skills | 2.37 | 3.57 | 2.13 | 1.80 |
| Pillar C | Access to finance | 3.54 | 3.56 | 3.87 | 3.86 |
| Pillar D | Public procurement | 2.80 | 3.15 | 2.92 | 3.83 |
| | Standards and regulations | 3.60 | 3.83 | 3.96 | 2.80 |
| | SME internationalisation | 2.91 | 3.58 | 2.82 | 2.98 |
| Pillar E | Business Development Services | 3.06 | 3.57 | 3.27 | 4.10 |
| | Innovation policy for SMEs | 3.00 | 3.09 | 2.39 | 2.48 |
| | Green economy policies for SMEs | 2.51 | 2.81 | 2.80 | 2.43 |

Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Table 10.2. Implementation progress on SME Policy Index 2020 policy reforms – Armenia

| Priority reforms outlined in the SME Policy Index 2020 | Key reforms implemented to date |
|---|---|
| **Pillar A – Responsive Government** | |
| Finalise and adopt a comprehensive, long-term SME strategy.<br>Assess impact of the special tax regime for microenterprises and family businesses.<br>Elaborate action plan for e-government strategy with open-data approach.<br>Streamline insolvency legislation and introduce prevention measures.<br>Implement a comprehensive and proactive second-chance strategy. | Adoption of a national SME Development Strategy for 2020-2024.<br>Expansion of range and accessibility of e-government services.<br>Simplification of company registration procedures.<br>Adoption of a National Digitalisation Strategy for 2021-2025.<br>Amendment of the Law on Bankruptcy in 2020. |
| **Pillar B – Entrepreneurial Human Capital** | |
| Integrate the entrepreneurship key competence into the curriculum and develop an entrepreneurial mindset.<br>Introduce active teaching and learning methods as well as pre- and in-service training for teachers and school/university managers.<br>Improve co-operation between education institutions and businesses through private sector involvement in skills intelligence collection and analysis and mandatory practical experience for all learners.<br>Update the women's entrepreneurship support strategy and set up a structured policy partnership.<br>Establish a system for collecting and analysing SME skills intelligence. | Integration of entrepreneurship into the curriculum and reflection of it in the learning outcomes of the state standards of general education.<br>Training from 2021 to 2022 for all teachers in general education on technology and entrepreneurship for grades 2-7 and 10-11.<br>Implementation by higher education institutions (HEIs) of entrepreneurial learning in different faculties.<br>Development of a *Platform for Women's Economic Empowerment* targeting women's entrepreneurship and employment.<br>Planning of women-specific initiatives, including the implementation of preferential interest rates, small grants, and women-only investment readiness programmes.<br>Awareness-raising campaigns conducted. |
| **Pillar C – Access to Finance** | |
| Complete reforms to insolvency / restructuring legal framework to strengthen creditor rights and promote corporate recovery.<br>Establish an information platform with details about financial products relevant to business owners. | Ongoing implementation of the new capital markets development strategy.<br>Launch of an Economic Modernisation Program for interest rate subsidies on loans and leases to purchase modern (new) equipment.<br>Adoption of a new regulation on investment-based crowdfunding.<br>Adoption of the Financial Literacy Strategy for 2021-2025. |
| **Pillar D – Access to Markets** | |
| Transfer institutional knowledge/capacity to Business Armenia's successor.<br>Enhance provision of export support and promotion services to SMEs.<br>Expand conformity assessment services and ensure competition between domestic conformity assessment (CA) bodies.<br>Work towards international recognition for national accreditation body.<br>Increase use of e-procurement and promote the use of award criteria.<br>Build contracting authorities' capacity for wider competition / transparency.<br>Analyse issues SMEs face in public procurement and address them with guidelines and training for contracting authorities and prospective tenderers. | Modernisation of prior institute into National Body for Standards and Metrology (ARMSTANDARD).<br>Development of annual state standardisation programmes for 2020-23.<br>Improved services on standardisation, metrology, and conformity assessment.<br>Preparation of the application for an EA Multilateral Agreement signature status for the international recognition of accreditation system.<br>Mandatory use of e-procurement and possible use of e-auctions.<br>Provision of trade insurance services by the Export Insurance Agency of Armenia (EIAA). |
| **Pillar E – Innovation and Business Support** | |
| Broaden the palette of policy tools available to support innovative companies beyond the IT sector.<br>Develop linkages between research institutions and the business sector.<br>Develop an innovation strategy and action plans to increase co-ordination among different actors in the innovation ecosystem.<br>Improve monitoring of current support programmes, measuring the impact of support programmes (particularly business development services, or BDS) on SME performance.<br>Tasking an agency with outreach to SMEs to promote green practices.<br>Implement a plan to support SME greening. | Pilot project to collect data on SME adoption of digital technologies.<br>Creation of a Ministry of High-Tech Industry (MoHTI) programme to help innovative start-ups and research teams to develop and commercialise their ideas.<br>New set of indirect financial incentives to modernise the economy (Government Resolution 106-L, support for loan and leasing agreements to purchase new machinery and equipment).<br>Inclusion of energy efficiency measures in the 2022-2030 Programme on Energy Saving and Renewable Energy. |

## Context

### *Economic snapshot*

Despite Russia's war of aggression against Ukraine and Armenia's exposure to the Russian economy, the country experienced unexpectedly strong GDP growth of 12.6% in 2022. This was driven largely by investment and strong domestic consumption, as well as a robust expansion of the tertiary sector, including tourism, financial services and real estate (EIU, 2023[1]). This sustained the economic rebound that followed the contraction (-7.2%) in 2020 due to the COVID-19 pandemic.

Economic growth has been supported by large capital inflows, owing to a substantial movement of businesses and people from Russia, around 39,000 of whom sought long-term residence (Sargsyan, 2022[2]). This inflow of people boosted the real estate sector, driving up rental prices and fuelling growth in the construction and services sectors. Armenian exports of goods grew 75% in 2022, as regional supply chains and trade flows found new configurations following the onset of the war (Central Bank of Armenia, 2023[3]). Although a sharp in food and energy prices accelerated pre-existing inflationary pressures, these eased in the second half of 2022, as monetary policy tightened and fiscal performance exceeded expectations (IMF, 2022[4]). Nonetheless, the economy remains highly dollarised, which continues to make the country vulnerable to external shocks resulting from currency fluctuations.

In 2022, industry and agriculture accounted for 18.5% and 10.4% of Armenia's GDP, respectively, with the relative weight of the latter in the economy, steadily decreasing in the last decade. At the same time, the information and communications technology (ICT) sector has been rapidly expanding in recent years, compounded in 2022 by an influx of capital and skilled labour from Russia, particularly in the IT and digital services sectors. Only a month following the outbreak of the war in February 2022, 268 Russian citizens registered firms and 938 individuals obtained official status as entrepreneurs (OECD, 2023[5]). In 2022, the ICT sector grew by over 20% and generated 4.5% of Armenia's GDP with the potential of growing further with the inflow of high-skilled specialists (Central Bank of Armenia, 2023[6]).

However, the sector is highly export-oriented and thus sensitive to fluctuations in the foreign currency market. For example, the appreciation of the Armenian dram in 2022 resulted in decreasing competitiveness for Armenian IT firms, which prompted the government to introduce a dedicated support package for affected companies (Ministry of High Tech Industry of the Republic of Armenia, 2022[7]). These policy efforts follow a period marked by a significant increase in the share of businesses that have started or increased online business activity – during COVID-19, this was the case for 48% of small businesses, 53% of medium-sized enterprises and 68% of large firms (World Bank, 2021[8]). Hence, Armenia's steps to support its ICT sector, particularly IT firms, stem from the importance of accompanying the expansion of its digital business environment.

Despite the recent macroeconomic trends, to which the "one-off" positive shocks described above have significantly contributed, several socio-economic challenges persist, including high unemployment (13% in 2022) and poverty (26.5% in 2021), as well as low productivity growth (Armstat, 2023[9]). Exports are concentrated in terms of both products – mainly metals such as copper, gold, and iron, as well as tobacco and alcoholic beverages – and destinations, as nearly one-third of exports in 2021 went to Russia (Armstat, 2022[10]).

## Table 10.3. Armenia: Main macroeconomic indicators, 2018-22

| Indicator | Unit of measurement | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|
| GDP growth* | Percent, year-on-year | 5.2 | 7.6 | -7.2 | 5.7 | 12.6 |
| Inflation* | Annual percent increase, consumer prices | 2.5 | 1.4 | 1.2 | 7.2 | 8.7 |
| Government balance[1]* | Percentage of GDP | -1.8 | -1 | -5.4 | -4.6 | -2.1 |
| Current account balance** | Percentage of GDP | -7.2 | -7.1 | -4.0 | -3.5 | 0.8 |
| Exports of goods and services** | Percentage of GDP | 39.4 | 41.4 | 29.8 | 35.3 | 47.7 |
| Imports of goods and services** | Percentage of GDP | 53.1 | 54.8 | 39.7 | 43.8 | 50.7 |
| FDI net inflows** | Percentage of GDP | 2.1 | 0.7 | 0.5 | 2.6 | 5.1 |
| General government gross debt* | Percentage of GDP | 51.2 | 50.1 | 63.5 | 60.2 | 49.3 |
| Domestic credit to private sector** | Percentage of GDP | 55.5 | 60.2 | 72.2 | 61.8 | 52.6 |
| Unemployment[2]** | Percentage of total active population | 13.2 | 12.2 | 12.2 | 12.7 | 12.6 |
| Nominal GDP* | USD billion | 12.5 | 13.6 | 12.6 | 13.9 | 19.5 |

[1] General government net lending/borrowing.
[2] Modelled ILO estimates.
Source: * (IMF, 2023[11]); ** (World Bank, 2023[12]); both accessed May 2023

### Box 10.1. Armenia's policy support for SMEs during the COVID-19 pandemic

In response to COVID-19, Armenia adopted 25 anti-crisis measures to support households and businesses.

**Financial support**

Measures to support enterprises include:

- Loans with preferential conditions to pay for salaries, equipment, food imports and raw materials, as well as breaks on taxes, duties and utilities.
- Sector-specific programmes:
  - The tourism, agriculture, food, and manufacturing sectors could benefit from loans of AMD 2.5 to 50 million (EUR ~6 000 to 118 000) with a six-month grace period and no interest during the first two years, and a 12% rate applied in the third year. Other sector-specific measures include:
  - Interest rate subsidies and co-financing mechanisms for agricultural entities and co-operative farms.
  - Loans with full interest subsidies for grape suppliers and brandy and wine companies.
  - Covering 75% of the outstanding interest on loans for transport companies in tourism until March 2021.
  - One-time grants for entrepreneurs in the IT sector and interest-free loans for individuals starting a business.

**Regulatory flexibility**

In 2020, the government launched temporary depreciation acceleration and corporate income tax advance payments, with the former operating only for 2020. The corporate income tax was reduced from 20% to 18% and the flat personal income tax rate was set at 23% and then reduced to 20% in 2023.

**Workforce support**

Job retention was encouraged through wage subsidies:

- One-time grants for businesses with 2-50 employees to cover the salary of every fifth employee.
- For tourism-related enterprises that have maintained over 70% of their staff or 25% of payroll, wage subsidies covered the salaries of every third employee for a period of nine months.

**Market support**

To promote innovative business plans, the Ministry of Economy introduced support for competitive entrepreneurial ideas developed by beneficiaries seeking to start their business. In March 2022, businesses in Armenia were offered subsidies for loans to buy new equipment and machinery.

**Measures to improve access to digital infrastructure**

The Ministry of Economy conducted 55 training programmes targeted at SME skills development, including the development of online delivery tools and digital literacy training. Within the framework of Enterprise Europe Network, consultancy and information services were made available to SMEs.

Source: (The Government of the Republic of Armenia, 2023[13]).

The business environment has markedly improved, as the government has pushed through a number of reforms, including those designed to increase the ease of starting and doing business. However, businesses still face regulatory bottlenecks and general inefficiencies within the government bureaucracy (ITA, 2022[14]). In addition, Armenia's relatively small market size and landlocked status tend to cap opportunities for economic growth. High transport costs and frequent delays at the Georgia-Russia crossing point, on which Armenia is highly dependent, constitute a choke point for Armenian trade. Since 2018, Armenia has taken steps to combat corruption, including establishing a new anti-corruption committee, strengthening the law on enforcement agencies, and creating a new anti-corruption court.

### *SME sector*

The definition of *micro, small and medium enterprise* (MSME) in Armenia has not changed since 2011. In line with the EU definition, it is based on three criteria: employment, turnover and balance sheet (Table 10.4).

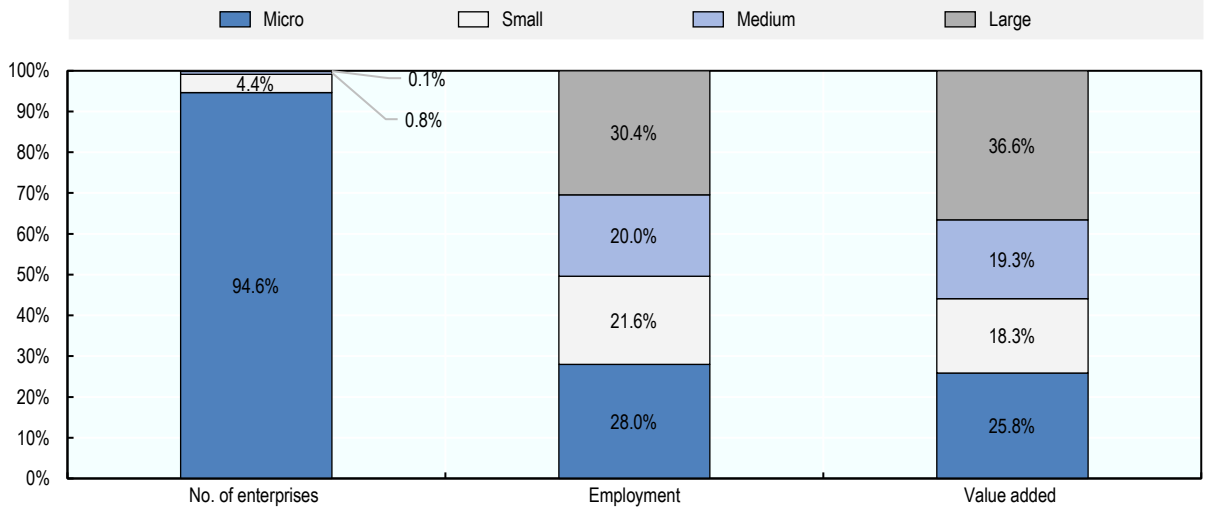
**Table 10.4. Definition of micro, small and medium enterprises in Armenia**

| | Micro | Small | Medium |
|---|---|---|---|
| Employment | < 10 employees | < 50 employees | < 250 employees |
| Annual turnover | ≤ AMD 100 million (EUR ~237 138) | ≤ AMD 500 million (EUR ~1 185 690) | ≤ AMD 1 500 million (EUR ~3 557 070) |
| Balance sheet | ≤ AMD 100 million (EUR ~237 138) | ≤ AMD 500 million (EUR ~1 185 690) | ≤ AMD 1 000 million (EUR ~2 371 380) |

Note: Exchange rate as of 28 September 2023 (OANDA, n.d.[15]).
Source: Amendments to the Law on State Support of Small and Medium Entrepreneurship (Legal Information System of Armenia, 2011[16]).

According to 2021 data, SMEs comprise almost 99.9% of all enterprises in the business sector, with micro-enterprises constituting 94.7%. SMEs account for 69.6% of total persons employed and generate up to 63% of value added (Figure 10.2).

**Figure 10.2. Business demography indicators in Armenia, by company size (2021)**



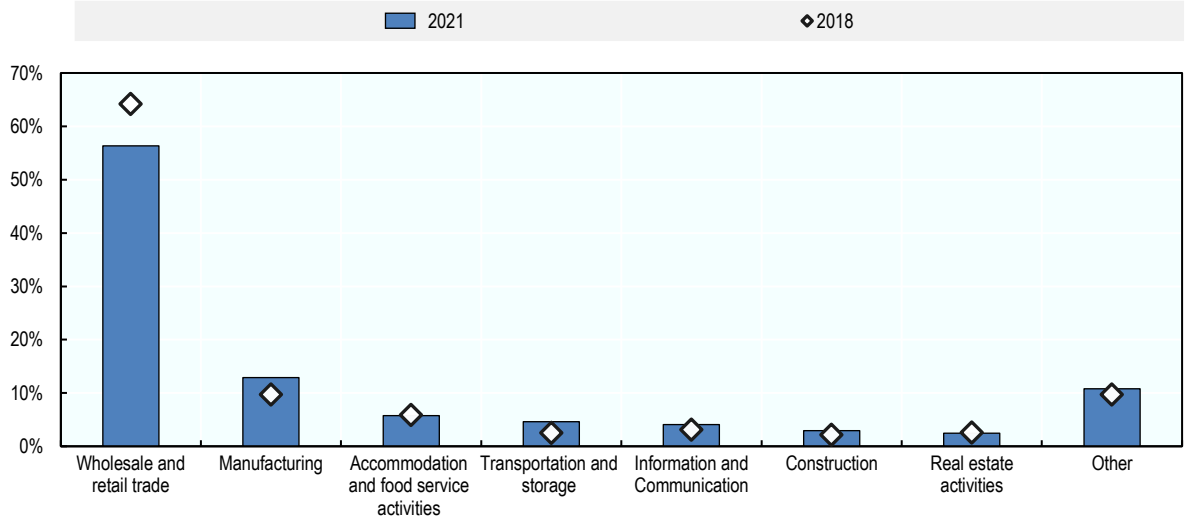

Source: (Armstat, 2022[17]).

StatLink https://stat.link/uzd9e1

Most SMEs are concentrated in low-value-added activities, with 56% operating in wholesale and retail trade (Figure 10.3). While the shares of SMEs in most economic sectors experienced minimal changes between 2018 and 2021, the share in the wholesale and retail sector notably decreased (by 7.8 percentage points), while the share in manufacturing increased (by 3.1 percentage points).

### Figure 10.3. Sectoral distribution of SMEs in Armenia (2021)

Share of SMEs, by type of economic activity




Note: "Other" includes the following sectors: administrative and support service activities, real estate activities, construction, repair of computers, mining, energy and water supply.
Source: (Armstat, 2022[17]).

StatLink https://stat.link/0zavfi

## SBA assessment by pillar

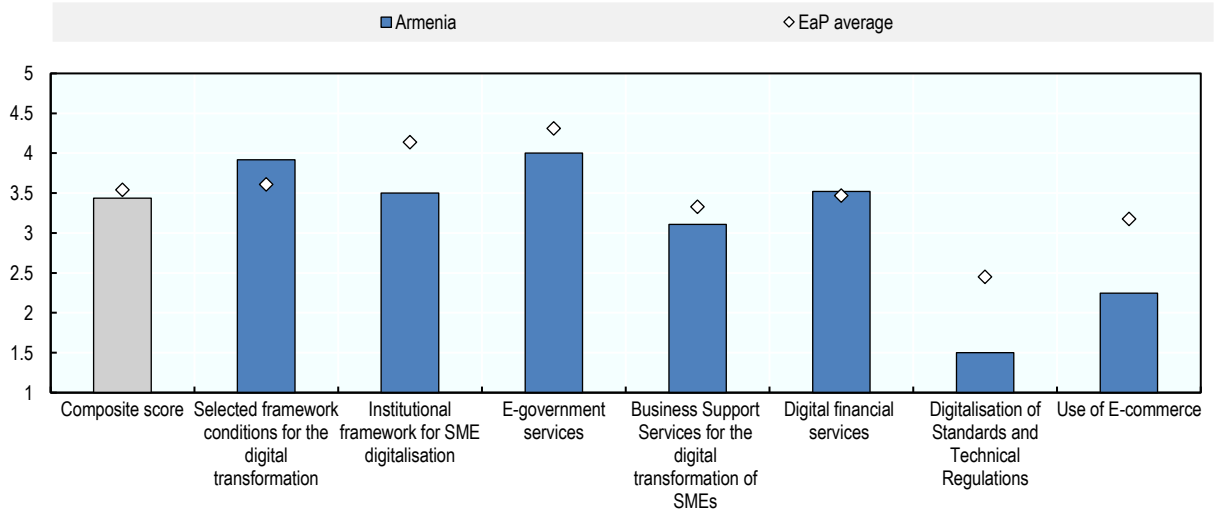
### *SME digitalisation policies*

Creating an environment conducive to the digital transformation of SMEs requires a comprehensive policy approach based on sound framework conditions for the digital economy as well as targeted support to help SMEs reap the benefits of digital solutions. Framework conditions refer to pre-requisites for the digital transformation, such as affordable access to high-speed broadband, a satisfactory level of digital literacy among citizens, and a well-co-ordinated and coherent policy approach and governance system for digital policies. In the context of SME development, those fundamentals need to be complemented with specific business support services, digital financial services for SMEs, and tailored support to engage in e-commerce to reach new markets.

Reflecting the multi-faceted nature of the topic, this round of SBA assessment evaluates EaP countries' policy approaches to SME digitalisation through i) a dedicated pillar on selected framework conditions for the digital transformation, as well as ii) six new sub-dimensions, incorporated in the pre-existing dimensions of the SBA assessment, to delve deeper into specific thematic policies to foster the digital transformation of SMEs. The weighted average of the scores for the new pillar and digitalisation-oriented sub-dimensions results in a composite score for SME digitalisation policies presented below (Figure 10.4)[1].

Overall, Armenia reaches a composite score of 3.44, close to the regional average. The country's performance is driven by a strong policy framework for digitalisation, i.e. the ongoing national digital strategy and related provisions planned to support SMEs – although the institutional settings for SME digitalisation remain less developed than in EaP neighbours so far. Armenia has also made further progress in increasing the provision of e-government services and digital financial services are being introduced, constituting a pillar of the Central Bank's general development strategy. E-commerce and digitalisation of standards and technical regulations appear as the weakest areas: although they are both embedded in the national digital strategy, full implementation of concrete measures has yet to materialise.

## Figure 10.4. Scores for SME digitalisation policies in Armenia




Note: Further details on the assessment and calculation methodology can be found in the "Assessment framework" section in the Digital Economy for SMEs chapter, in the "Policy framework, structure of the report and assessment process" chapter and in Annex A. Additional information on institutional framework for SME digitalisation and e-government services can be found in Pillar A; on digital financial services in Pillar C; on use of e-commerce in Pillar D; and on Business support services for the digital transformation of SMEs in Pillar E.

StatLink https://stat.link/rnhctw

The following section details Armenia's performance in developing selected framework conditions for the digital transformation, while more information on digitalisation-oriented sub-dimensions can be found in the sections on the pillars they respectively belong to.

### *Selected framework conditions for the digital transformation*

Individuals and firms, notably SMEs, cannot fully reap the benefits offered by the digital transformation without the existence of robust framework conditions, such as comprehensive digitalisation policies, access to high-speed Internet and well-rounded ICT skills among the population. Accessible, affordable and stable broadband connection is indeed the *sine qua non* to ensure widespread participation of citizens and businesses in the digital economy, and to stem the widening of the connectivity gaps between urban and rural territories and between firms of different sizes. Furthermore, fostering digital skills development at all stages of life (through formal education and lifelong learning initiatives for adults) is essential to help the working-age population acquire the skills they need to embark on the digital transformation, produce tech-savvy consumers and build a talent pool of IT specialists.

### *National digital strategy*

Digitalisation is a policy priority for the government. In 2021, the *Digitalisation Strategy of Armenia for 2021-2025* (DSA) was adopted, aiming at ensuring i) efficient, transparent and data-driven public administration; ii) economic modernisation and increased competitiveness through digital platforms and smart solutions; and iii) development of digital skills and widespread use of digital solutions in society. The strategy aims to digitally transform government, business and society and covers cybersecurity, data policies, broadband connectivity, digital skills and legislation. It also entails provisions designed to accelerate SME digitalisation. In particular, the document aims at raising awareness of digital technologies across the private sector; fostering SMEs' uptake and use of digital solutions by various means (including events, legislative incentives and consulting programmes); and providing automated software-as-a-service (SaaS)-type solutions (accounting, personnel management, warehouse management, etc.) on a public cloud platform (free or on preferential terms). Additional measures are planned to develop e-commerce and innovative solutions.

The DSA's Action Plan is accompanied by a dedicated budget. During 2021-25, it is planned to allocate at least AMD 20 billion (EUR ~47 mln) for the implementation of the DSA. Moreover, Armenia has worked to build a multi-stakeholder approach to digitalisation policies: in 2019 the government established a "Digitalisation Council" that brings together the deputy prime minister; the head of the Prime Minister's Office; the Ministers of Economy and High-Tech Industry; the deputy ministers of the Ministry of High-Tech Industry (MoHTI); the Minister of Education, Science, Culture and Sports; the First Deputy of the State Revenue Committee; and the CEO of Ekeng CJSC and the head of the SDG Innovation Lab in Armenia. The draft strategy also benefitted from public feedback through the e-draft.am platform[2] and from reviews by World Bank experts. With regard to implementation, the MoHTI is tasked with a co-ordination role, and the strategy foresees the establishment of working groups of working groups (made up of representatives from the IT sector) to conduct consultations around general strategic and individual digitisation projects. The Central Bank is also closely involved in the implementation process. Finally, the Information Systems Agency of Armenia (ISAA) was established in 2022 to ensure an overarching vision for Armenia's digitalisation. The agency is responsible for the development of technological foundations and digital society in the country, providing technical resources, organisational capabilities, a legal/regulatory framework, and a platform for collaboration by relevant public stakeholders, as well as the private sector, to effectively foster digitalisation.

Monitoring and evaluation of the Strategy will be performed annually by the Audit Chamber.

The DSA foresees establishing key performance indicators (with associated targets) to facilitate this. However, while some of these indicators will allow for the assessment of progress in some areas, such as e-government and broadband connectivity (see below), they do not capture in areas like SME digitalisation or digital skills. Moreover, some of the selected indicators could be improved. For example, the Action Plan sets the improvement of Armenia's ranking in the UN E-Government Development Index as a target, but such change in ranking is contingent on other countries' performance; taking into account the score instead of the ranking would allow for a more accurate depiction.

Moving forward, Armenia will need to closely monitor the implementation of its DSA, ensuring that roles are clearly defined, and that funding is predictable and secure. Indeed, the implementation report published in March 2023 revealed that targets have been only partly met. Continued co-ordination with all relevant stakeholders should be enhanced – encompassing the Ministry of Labour, local authorities, and non-governmental stakeholders such as businesses, the civil society and trade unions. The latter are indeed crucial to shaping digitalisation policies and supporting their implementation (Gierten and Lesher, 2022[18]). Finally, Armenia should consider collecting additional data on the digital transformation to help monitoring policy impact – the OECD Going Digital Framework and its indicators can serve as a useful example.

### *Broadband connectivity*

The DSA provides for the development of broadband connectivity and digital services and aims to expand access in remote regions. As a follow-up to this document, a dedicated *National Strategy for Broadband Connectivity* is currently being developed. Indeed, the COVID-19 pandemic and resulting increase in demand for Internet services and telecommunication prompted the government to update its agenda for broadband connectivity. The MoHTI mapped existing and operating optical-cable transmission networks in the public and private sectors, identifying their capacities and corresponding network topologies; it also assessed demand in the different regions of Armenia. The conclusions fed into a draft strategy titled "Ensuring access to broadband Internet connectivity in the territory of the RA 2022-24", which was then revised by a dedicated working group established in 2022. The draft was published on the e-draft platform in April 2022 and is yet to be approved.

There have been some considerable improvements in broadband uptake and quality in Armenia in recent years. In 2021, Armenia had a fixed broadband penetration rate of 16.7% (with a 60% increase between 2016 and 2021, i.e. the largest increase in EaP countries), and a mobile broadband penetration rate of 90.6% (+61% over the same period). Meanwhile, close to 79% of Armenians use the Internet, +22% since 2016. Armenia also saw the development of high-speed networks, with fourth-generation-plus (4G+) technology for mobile networks currently covering 100% of settlements. In 91% of the settlements, the 4G+ coverage of at least two operators' mutually penetrable mobile communication technology is available. Further efforts are planned, with the DSA providing for the construction and improvement of a fibre optic network. In December 2022, the median speed of a fixed broadband download was 40.1 megabits per second (Mbps) (Armenia ranking 99), while the median speed of a mobile Internet download was 24.7 Mbps (Armenia ranking 82) (Ookla, 2023[19]). Overall, data reveal noteworthy progress in bridging the digital gap between urban and rural areas in Armenia in recent years. The DSA further aims at providing 80% of households in both rural and urban areas with access to high-speed Internet and e-government services by 2025. Additional measures are foreseen in the draft broadband strategy to increase access to digital services for several target groups, such as individuals with disabilities.

However, despite the recent increases, uptake in broadband subscriptions remains limited, especially for fixed broadband, which is lower than EaP, EU and OECD peers (21% for EaP countries on average, and about 35% for OECD and EU median values). This difference can be partly explained by persisting Internet affordability issues: while prices for mobile broadband have dropped to 1% of gross national income (GNI) per capita in 2021, prices for fixed broadband in Armenia are still above the International Transport Union's (ITU) 2% target, reaching 3.5% GNI per capita in 2021 – the highest value in the EaP region. Moreover, assessment and monitoring of digital divides are impeded by the lack of disaggregated data on subscriptions, coverage and quality of service. Data on firms' broadband uptake and speed, for instance, are not available.

Moving forward, Armenia could further encourage broadband uptake by improving Internet affordability, especially for fixed broadband, and improving data collection to allow for accurate and regular assessments of remaining digital divides, notably on businesses' access to high-speed Internet. Providing access to open and reliable data on subscriptions, coverage and quality would also enhance consumer choice by helping them making informed decisions, while incentivising providers to improve network quality. Finally, Armenia should consider conducting multi-stakeholder consultations throughout the development and implementation of its upcoming broadband strategy; currently, such consultations (which involve non-governmental representatives) are usually held only on an ad hoc basis. Some national telecom operators (MTS Armenia, Ucom, Telecom Armenia) participated in stakeholder consultations organised during the development of the broadband strategy, but such exchanges should continue moving forward – and should also involve consumers, regulatory authorities, and all levels of government.

### *Digital skills*

The DSA acknowledges that there is a shortage of professionals with digital skills in the private and public sectors, primarily due to a mismatch between education and the labour market. In 2020, only one-sixth of the population used e-government tools, mostly for information purposes, and only 5% of the population used Internet banking – a share significantly lower than in the EU and Georgia, for instance (World Bank, 2020[20]). According to the UN E-Government Survey 2022, Armenia ranks 64th out of 193 countries, slightly behind Georgia but ahead of Moldova.

Well aware of this pressing issue, Armenia has included digital skills as one of the priorities of the DSA. The latter outlines a plan to introduce in-depth courses in schools as an essential step for the development of digital literacy. Moreover, Armenia has planned various measures and educational programmes for different age and social groups – such as people with special needs (as an important means of social and professional integration), women and girls, and residents of communities and remote villages – for whom courses will be organised, along with awareness-raising activities on e-government services. The DSA foresees, for instance, the creation of e-service centres across the country and online courses for seniors and those without advanced technological skills, while civil servants will benefit from training in digital security issues. In terms of recent achievements, Armenia has included digital competence as a key competence in the national education curricula at all education levels.

Armenia's approach to digital skills benefits from the active involvement of non-governmental stakeholders. While digital skills policies are implemented by the MoHTI, the Ministry of Education, Science, Culture and Sports, the Ministry of Economy, the Central Bank, and the ISAA, representatives from the private sector have launched several successful initiatives to develop digital talents. In particular, there are a number of cases of co-operation between higher education institutions and businesses on these topics. The TUMO Labs education programme, for instance, connects tech companies with universities, offering students opportunities to acquire skills in science, technology, engineering, and mathematics (STEM) through guided self- and project-based learning. The centre has experienced significant success, with approximately 95% of participants finding high-paying jobs in the field upon graduating from the TUMO-led *42 Yerevan initiative* (42 Yerevan, 2023[21]) (see Box 4.2 in the "Digital Economy for SMEs" chapter).

The government is supporting this impetus through such initiatives as the recently launched *Private Sector Cooperation of the Higher Education Institution for the Training of Specialists*, as part of its efforts to develop a talent pool of IT specialists in the country. The programme foresees conducting a training-needs analysis of IT specialists, developing appropriate training courses, further promoting HEI-private sector co-operation, establishing new technological centres/laboratories in and outside Yerevan, and training 1000 specialists in engineering, cyber security, IT and blockchain through intensive 3-6 month courses.

However, Armenia's achievements in digital skills assessment and anticipation remain relatively scarce. Data on digital skills levels (across individuals of different target groups and businesses) are not regularly collected and analysed. The EU4Digital benchmark of digital skills indicators available, published in 2020, revealed that Armenia lags behind its EaP peers in this regard (EU4Digital, 2020[22]). This significantly impedes policy monitoring and evaluation: despite its provisions for digital skills development, the DSA does not set specific targets to monitor progress in this regard, only foreseeing an increase to at least 60% of people 16-65 years old using electronic tools. Digital skills anticipation exercises are also at a nascent stage, although Armenia benefits from some promising donor-funded ad hoc initiatives – such as the Edu2work platform, which provides fresh insights on skills demand and informs policymaking, notably for labour market policies. There is, nonetheless, no systemic country approach for now.

Moving forward, Armenia could i) ensure the involvement of all relevant stakeholders and co-ordination between the different public and private initiatives, raise awareness of the support available and monitor and evaluate impact; ii) improve digital skills assessment and anticipation tools – notably by collecting data

and adopting a digital competence framework on the basis of which the skills acquired could be benchmarked and certified (in line with the EU's Digital Competence Framework, or DigComp); and iii) further promote digital skills development among businesses, especially small ones, as few provisions have been planned and implemented in that direction so far – even though the lack of digital literacy is evidently a major obstacle to SME digitalisation.

## *Pillar A: Responsive Government*

### *Institutional and regulatory framework*

Armenia has been conducting a proactive SME policy since the early 2000s. However, despite significant progress between 2016 and 2019, further efforts to improve the institutional framework for SME policy, including regulatory reform, were put on hold in 2020, mainly due to the impact of the COVID-19 pandemic and increased political instability. Although the reform process resumed in 2022, it has produced mixed results.

#### Institutional setting

The mandate to design and co-ordinate SME policy is assigned to the Ministry of Economy. Until recently, the National Center for SME Development (SME DNC), established in 2002, was in charge of implementation, offering a wide range of support programmes through its headquarters in Yerevan and a network of 10 regional offices. In 2016, the Armenian government launched its first SME Development Strategy, covering 2016-18. Upon conclusion of the strategy, the Ministry of Economy commissioned an independent evaluation. In August 2020, a new national SME Development Strategy was approved for 2020-24, largely based on the recommendations emerging from the previous strategy's evaluation.

The new strategy has three key objectives: i) achieving a productivity growth averaging 3% per year during 2021-23 and 7.5% in 2024, ii) increasing employment in the SME sector by an average of 2.5% per year and iii) raising Armenia's score in the Global Entrepreneurship Index from 22.8 in 2020 to 40 in 2024, as a measure of improvements in entrepreneurial activity and business environment (GEDI, 2019[23]). The strategy also identified a set of measures designed to improve the competitiveness of the SME sector by developing the capacity and entrepreneurial culture of SMEs, facilitating SME access to markets, and providing a favourable institutional and legal environment for SMEs. An action plan for 2020-22 was also approved. However, the implementation of the strategy faced a very difficult start and was carried out only partially. During 2020-22, the plan was to spend AMD 8.8 billion (EUR ~21 mln) on the implementation of SME support activities, of which AMD 5.1 billion (EUR ~12 mln) was to be allocated from the state budget, with the remaining gap expected to be filled by donors. Overall, the current strategy remains largely unimplemented.

An additional disruptive element in the strategy implementation was the government's decision in 2022 to dismantle the SME DNC and transfer its mandate to mandate to two government bodies: the Department of Entrepreneurship (within the Ministry of Economy) and a different government agency, the Investment Support Center. The latter agency, now re-branded as Enterprise Armenia, is therefore in charge of SME policy and investment promotion, although the allocation of resources between the two tasks is not clear. The restructuring also led to the closure of the network of SME DNC local offices and the concentration of all SME development activities in the capital, while the government ponders various options for supporting local development. Nevertheless, as of May 2023, the government plans to establish a new entity to support SME development, although details on its mandate, the resources, and timeline for its establishment are yet to be defined.

Given the changes in the regional geo-political context, the emergence of a new ICT sector, the re-orientation of trade flows and the establishment of Enterprise Armenia, the Ministry of Economy is currently working on a review of the SME Development Strategy and its extension to 2026. As the strategy and

action plan for implementation are under review, planned monitoring and evaluation functions are also under consideration.

The informal sector has a relevant presence in Armenia, but the current SME Development Strategy presents no specific actions to limit its size. Informality is mainly seen as a tax compliance issue.

### Legislative simplification and RIA

No significant changes have occurred with regards to the implementation of regulatory reforms and the application of regulatory impact assessment (RIA) since the previous SBA assessment. Nevertheless, reform of the regulatory framework remains a long-term priority for the government. Over the past decade, the number of redundant regulations governing entrepreneurial activity has decreased significantly. However, the process of regulatory reform is far from complete, as less than 25% of all primary and secondary legislation having an impact on business activities is estimated to have been reviewed so far. Since 2019, Armenia has also taken steps to regularly implement RIA as part of its legislative and regulatory processes. According to the current legislation, an RIA of a draft law or a draft government decision must be conducted if it can have a significant impact on the business environment. The RIA should cover the following aspects: i) economic, including business environment and competition; ii) public finance; iii) social; iv) health; and v) environmental. In practice, RIAs are routinely conducted as part of the regulatory reform process, but no SME test has been applied so far.

### Public-private consultations

The Armenian government has a long-standing practice of frequent public-private consultations. The Investment Council of Armenia (ICA), in particular through the SME Development Council, serves as a broad platform for public-private dialogue (PPD) on business-oriented legislative reforms between the government and SME associations. Membership in the SME Development Council is open to all relevant associations and non-governmental organisations (NGOs). However, the final list of members is approved by the prime minister. Regular meetings of the SME Development Council, chaired by the Minister of Economy, and of the Investment Council, chaired by the deputy prime minister, are conducted every two months, to guarantee a regular involvement of the Ministry of Economy.

All draft laws and draft decisions of the government are subject to public consultations, which are conducted through a single website: www.e-draft.am.

Public-private dialogue has been further enhanced with the launch, in December 2022, of a new initiative supported by USAID, aiming at improving PPD practices in relation to the approval of several legislative changes – for instance, the amendments to the Civil Code, the Tax Code and the Banking and Finance Laws.

### Institutional framework for SME digitalisation

The SME Development Strategy (2020-2024) calls for an acceleration of SME digitalisation and indicates that the government is committed to supporting SMEs' digital presence on commercial platforms. Actions related to those objectives were included in the Action Plan related to the strategy implementation, and in 2021 AMD 50 million (EUR ~118 000) was allocated for technical support to the digital transformation of export-oriented SMEs, with most of the funding provided by donors.

In addition, the *Digitalisation Strategy of Armenia for 2021-25* outlines a programme to promote the use of digital solutions among SMEs. In particular, applications such as the SaaS-type automated solutions (accounting, human resource management, warehouse management, etc.) will be provided on a public cloud platform for free or on preferential terms. However, an operational agency supporting SME digital transformation has not yet been identified.

### The way forward

To continue improving its institutional and regulatory framework for SMEs, Armenia should complete the revision and update of the current SME Development Strategy. Its objectives should be consistent with the recovery from the crisis related to the COVID-19 pandemic and with the structural changes occurring in the country's economy, i.e. the growth of the ICT sector. The government should identify an agency with a clearly defined mandate to support SME development, and ensure that adequate human and financial resources are allocated in line with the revised objective of the SME Development Strategy. In addition, Armenia should ensure that SMEs located outside the capital continue to have access to business support and training services and conduct those activities in the framework of a revised local development strategy. To conclude, Armenia should extend the application of RIA to all relevant primary and secondary legislative acts and introduce an SME test.

## *Operational environment for SMEs*

The improvement of the operational environment has been a main priority for the government since the early 2000s. While noticeable progress has been achieved in several areas, Armenia's scores in all sub-dimensions related to the improvement of the operational environment for SMEs presented in the 2020 EaP SME Policy Index have been below the EaP average, apart from the dimension related to company registration.

Since 2020, Armenia has made significant efforts to expand the range and the accessibility of e-government services. It has also continued to make incremental progress over the other sub-dimensions by further simplifying company registration procedures and by introducing a new simplified tax regime for micro-entrepreneurs.

### E-government services

In 2021, the government adopted the Digitalisation Strategy of Armenia through 2025, placed under the supervision of the Ministry of High-Tech Industry (see above), that established ambitious goals for promoting e-government services. Targets were set for promoting the use of digital solutions, encouraging e-commerce, and enhancing the digital transformation at enterprise level. At the same time, following Russia's war of aggression in Ukraine, the country has received a significant inflow of IT experts from Russia which has contributed to the expansion of the ICT sector and increased the country's technical capacity to implement ICT solutions. The government is offering an increasingly wide range of e-government services – including online filing of tax returns and social security contributions, e-licensing, e-cadastre, e-procurement, e-payments services, and e-registration of companies. All e-services can be accessed from a central bilingual portal at e-gov.am. In addition to online services, in 2020 the first unified office for public services was launched in Yerevan, providing a wide range of services to citizens and enterprises.

### Company registration

In recent years, Armenia has introduced some of the world's most efficient, transparent, and low-cost company registration procedures. Company registration continues to be a highly simplified and efficient process. All procedures can be conducted either online or through a physical "one-stop shop" system. As a result of the registration, the applicant receives a state registration number, a taxpayer identification number, and an account number along with a personal payment card for social payments.

All forms required for completing the registration process, including the standard articles of incorporation, are produced automatically during the registration process. In February 2021 amendments to the Law on State Registration of Legal Entities were approved, further simplifying the online registration process,

abolishing the online registration fee, and introducing a deadline for registration completion by public entities.

#### Business licensing

A comprehensive set of information on all licenses, including license applications, is available through the centralized e-licenses portal[3], which serves as a single-entry point for requesting licenses and permits. Over the previous four years, the number of licensed activities has expanded slightly due to public safety concerns. For example, the production and maintenance of medical equipment, all types of pre-school services, and some transport services are now subject to licenses.

#### Tax compliance procedures for SMEs

Tax administration is relatively simple, and tax returns can be filed online. In 2020, a new tax regime for micro-entrepreneurs came into force. Under this preferential tax system, taxpayers are exempt from all basic taxes and can hire an unlimited number of employees. Legal entities, individual entrepreneurs, and individuals can all operate under this tax system if their annual turnover does not exceed AMD 24 million (EUR ~57 000). Furthermore, at the beginning of 2020, the corporate income tax rate was reduced from 20 to 18%, and the flat personal income tax rate was set at 23%. A further reduction to 20% was applied at the beginning of 2023. A turnover tax has been introduced to replace value-added tax (VAT) and (or) corporate income tax for SMEs. To qualify for the turnover tax regimes, enterprises must have an annual turnover not exceeding AMD 115 million (EUR ~270 000). The turnover tax rate varies from 1.5% to 25% depending on the type of activity but is generally 5%. While the new tax regimes for micro-entrepreneurs and SMEs have reduced the tax burden and simplified tax compliance procedures, at the same time they may have also introduced incentives to hide part of the enterprise turnover in order to qualify for the new regimes, thereby increasing the size of the informal economy.

#### The way forward

To further improve the operational environment for SMEs, Armenia should i) conduct a review of the range of available e-government services and fill gaps related to the provision of good-quality services to SMEs; ii) improve co-ordination among public entities for the provision of e-government services, especially in areas where it appears to be weaker, i.e. business licenses and tax compliance; iii) systematically collect data on the use of e-government services by SMEs and take actions to increase their usage by improving SME digital skills and conducting promotional campaigns; and iv) calculate the effective tax rates imposed on different types of SMEs and make sure that tax incentives do not generate distortions and promote turnover and income under-declaration.

### *Bankruptcy and second chance*

Bankruptcy proceedings for legal and natural persons are governed by the Law on Bankruptcy adopted on 25 December 2006 and subsequently amended. The law formally provides for restructuring procedures, protection of creditors' rights, and discharge procedures, and it applies to private businesses as well as state-owned enterprises (SOEs). Bankrupt entrepreneurs can obtain a formal court decision declaring them non-fraudulent and thus excusable. The last amendment to the law in April 2020 introduced significant changes, such as the improvement of the regulatory system for insolvency practitioners with the creation of self-regulatory associations of practitioners under the control of the Ministry of Justice (MoJ), and the introduction of the electronic exchange of documents between the specialised insolvency courts, state and local authorities, and insolvency practitioners (EBRD, 2021[24]).

However, the legislation could be further improved to reach international standards (EBRD, 2021[25]). In particular, bankruptcy procedures and the operation of insolvency courts could be streamlined by

introducing out-of-court debt restructuring procedures as a less costly alternative to formal bankruptcy proceedings.

Moreover, Armenia has not substantially advanced since 2020 as regards the implementation of preventive measures to assist entrepreneurs in financial distress. The government could consider introducing pre-insolvency tools – such as public awareness campaigns highlighting available support, publicly sponsored advisory services, and early-warning systems – to support entrepreneurs in the early stages of financial difficulties. Additionally, Armenia could consider implementing a dedicated policy strategy or information campaign to promote "second chance" for bankrupt entrepreneurs seeking a fresh start. To this end, the government should also remove existing barriers for failed entrepreneurs to re-enter the market (e.g. the restriction imposed by the Armenian Tax Code, according to which an entity that declares bankruptcy is prevented from working under the preferential tax regime for five years). To conclude, activities to monitor and evaluate both bankruptcy-prevention measures and survival-and-bankruptcy procedures remain limited, and the government could consider developing monitoring and evaluation practices to increase the efficiency and effectiveness of its bankruptcy and prevention policy.

## *Pillar B: Entrepreneurial human capital*

### *Entrepreneurial Learning*

Entrepreneurial learning is part of several national official documents, including the *SME Development Strategy 2020-2024* and the *Gender Policy Implementation Strategy*. According to the action plan of the SME Strategy, Armenia planned to spend AMD 136 million (EUR ~320 000) on activities aimed at improving the entrepreneurial skills of entrepreneurs and employees of SMEs. As recommended in the SME Policy Index 2020, the new SME strategy broadened Armenia's approach to entrepreneurial learning by emphasising the need to promote the development of an entrepreneurial mindset (leadership, responsibility, proactivity, willingness to take risks) and related skills, such as teamwork and project management.

Currently, entrepreneurship is integrated into the subject "Technology" in grades 2-7, and as a dedicated topic in grades 10-11 and in all vocational education and training (VET) specialties. Accordingly, entrepreneurship as a key competence is reflected in the learning outcomes of the state standards of general education and all specialties of vocational education. Armenia has made further progress in teacher training since the last SBA assessment: the Ministry of Education, Science, Culture, and Sports collaborates with the NGO Junior Achievements of Armenia to promote entrepreneurship education in public schools, including training teachers and developing teaching materials. In 2021-22, all teachers in general education were trained in Technology and Entrepreneurship (for grades 2-7 and 10-11, respectively). Additional efforts are being provided in that direction with the support of GIZ.

With regard to higher education institutions (HEIs), several Armenian HEIs are now implementing entrepreneurial learning in non-business faculties and non-technological faculties, with donor support. For example, the State Academy of Fine Arts of Armenia implemented a Creative Entrepreneurship training programme in 2019, with the sponsorship of the British Council. The latter has also funded six "Creative Spark" partnerships in seven Armenian universities. Furthermore, some HEIs, such as the American University of Armenia, have been co-operating with businesses to promote entrepreneurial learning, although these cases remain limited to business faculties.

However, Armenia shows overall mixed progress since 2020. There is still no formal national policy partnership in place, and not all learners engage in at least one practical entrepreneurial experience. There have not been significant improvements in the ways entrepreneurial learning is promoted among the population, nor in career guidance. More emphasis could be put on non-formal learning. Despite a few ad hoc examples, education−business co-operation remains scarce – there is no systemic co-operation between SMEs and secondary schools (either in general education or in VET), and the topic remains

unaddressed in policy documents so far. Finally, the assessment reveals a lack of monitoring and evaluation: recommendations from the monitoring and evaluation of lifelong entrepreneurial learning activities are not integrated into further improvement of national policies, and students are not tracked after graduation.

Moving forward, Armenia should adopt a formal policy partnership on entrepreneurial learning and further foster non-formal learning. Building on existing efforts, teacher training could be strengthened by i) having pre-service teacher training institutions implement entrepreneurship key competence as a compulsory topic; ii) providing in-service teacher training covering entrepreneurship in VET institutions; and iii) providing training on the topic for school and university managers. Moreover, the successful cases of co-operation between HEIs and businesses could serve as an example to foster co-operation between general secondary schools and SMEs, to further promote entrepreneurial learning at all education levels. Finally, monitoring and evaluation could be improved, notably by tracking graduates.

### *Women's Entrepreneurship*

According to the Global Entrepreneurship Monitor's (GEM) 2020 report on Armenia, the share of women involved in entrepreneurship, despite being lower than that of men, is increasing (Global Entrepreneurship Monitor, 2020[26]). The report reveals that the motivation of men and women differs significantly, as more women start a business "to make a difference in the world," while men are rather motivated by "[creating] a large fortune or income" and "[continuing] the family tradition". However, both women and men creating a business are mostly subsistence entrepreneurs, choosing this path because job opportunities are scarce (Ameria CJSC, 2020[27]). An IFC study conducted in 2020 found that women-owned businesses tend to be younger and smaller. While both male and female entrepreneurs typically receive support from family members in their entrepreneurial endeavours, the pressures associated with running a household and caring for children remain major challenges for women entrepreneurs (IFC, 2021[28]).

Since 2020, Armenia has taken several measures to foster women's entrepreneurship. This topic is addressed in several policy documents, including both the SME Strategy and the *Gender Policy Implementation Strategy for 2019-2023* and their related action plans. Armenia is now working on developing a "Platform for Women's Economic Empowerment" training project targeting women's entrepreneurship and employment, with co-financing from the Ministry of Labour and Social Affairs, the Ministry of Economy and UNDP. The project seeks to empower at least 50 aspiring and 50 current women entrepreneurs, as well as 250 women with low economic capacity. As of December 2022, 209 aspiring and 54 current women entrepreneurs were participating in the training, according to the Ministry of Economy.

Additional women-specific initiatives have been planned, with various focuses – such as preferential interest rates foreseen in the SME strategy, small grants implemented by the SME Cooperation Association and UNDP in 2021 to encourage women's entrepreneurship in regions, and the Enterprise Incubator Foundation (EIF)'s women-only investment readiness programme. Moreover, some awareness-raising campaigns have been conducted, e.g. in conjunction with International Mathematics Day 2022 and the UNDP-led series of Accelerator #5 programmes,[4] which aim to inspire girls and women to engage in STEM fields.

Nevertheless, women's entrepreneurship policies would benefit from better co-ordination across public and private stakeholders. Current policy documents contain neither measures for strengthening the capacity of non-government organisations and networks active in the field, nor co-ordination measures between the different relevant ministries. Moreover, more could be done to raise awareness of the support available, e.g. by publishing information about government support for women entrepreneurs on a dedicated website. Finally, monitoring and evaluation remains limited: support policies and programmes are not monitored and evaluated, and there are no regular surveys being conducted on barriers to women's entrepreneurship.

Moving forward, Armenia could i) strengthen co-ordination across public and private stakeholders engaged in women's entrepreneurship policies, to foster a common assessment of women entrepreneurs' remaining needs, optimise efforts and ensure proper monitoring and evaluation of the initiatives' impact; ii) complement its support by addressing persisting yet overlooked issues, such as informality; and iii) improve monitoring and evaluation, e.g. by conducting regular surveys on barriers to women's entrepreneurship (building on the good GEM Monitor example). Beyond measures addressing women's entrepreneurship, Armenia could implement additional measures to foster gender equality, including a gender sensitivity check of existing and proposed policies affecting women entrepreneurs.

### *SME Skills*

Facilitating the development of current and future SME skills, together with allocating financial support for SME training programmes, is essential to tap into Armenia's entrepreneurial potential.

The SME State Support Annual Program, previously managed by the SME DNC, offered support in areas such as youth and women's entrepreneurship and internationalisation. However, following the restructuring of the SME DNC, responsibility for these initiatives has been re-distributed among separate organisations. The department of Entrepreneurship of the Ministry of Economy is now responsible for the provision of general information and training services for SMEs, while Enterprise Armenia is in charge of managing support in the framework of the Enterprise Europe Network. Within the framework of Action 9, over 2020-22 the Ministry of the Economy organised 55 skill-development training courses in which 601 SMEs participated.

Most of the SME/start-up skills development programmes, however, are delivered by NGOs, largely as a component of donor-funded projects. As a leading contributor to national skills intelligence, the Enterprise Incubator Foundation carries out a range of activities, such as digital and entrepreneurial training for SMEs, in schools, and for lifelong learning of adults. Overall, a wide range of accelerators and incubators have been developed to implement training and mentorship programmes. These include the IRIS Business Accelerator, the SAP Start-up Factory, the BANA Business Incubator, the Armenia Startup Academy, and the ImpactAim accelerators.

Similarly, in an apparent step forward since the last SBA assessment, some ad hoc training-needs analyses and skills-anticipation exercises have been conducted by international organisations and private consulting firms, supported by donors.

However, Armenia still lacks a national framework for the collection and analysis of data on SME skills. Despite some statistics being collected on SME participation in state-supported training, data on SME skills and needs is very scarce, and no analysis of SME skills data has been undertaken since the last assessment. No skills assessment and anticipation tools have been implemented yet. The scattered training and mentoring initiatives, implemented by various stakeholders, make it difficult to establish an overview of beneficiaries, and increase the risk of overlapping services. SMEs can also struggle to navigate between the training offers, to understand the differences and to select the most appropriate one(s) – indeed, there is no one-stop shop / web-based platform to help them identify training programmes. Some areas remain uncovered, such as greening – the Climate Change Tech Accelerator, which used to cover this area, was not re-conducted after 2020. Moreover, despite the COVID-19 pandemic, there has been very little progress in the development of online training (as recommended in 2020), and there is no example of digital learning methods being used. Finally, monitoring and evaluation of support programmes are still at a nascent stage, with no impact evaluation being conducted.

Moving forward, Armenia could increase co-ordination among business support service providers and donors to avoid overlaps and maximise impact. Enhancing collaboration between business associations already involved on the topic (such as the Chamber of Commerce and Industry) and other stakeholders (such as Business Armenia) would also help co-ordinate efforts and gather first-hand private sector views on persisting needs. In the medium/long term, the country should consider reducing its reliance on NGOs'

provision of upskilling and reskilling initiatives for SMEs to ensure support does not remain limited to basic training but offers opportunities for entrepreneurs at all stages of business development. Furthermore, raising awareness of the different training opportunities available would considerably help SMEs navigate between the different offers – e.g. through a single online portal. Publishing all available SME training events on an integrated website would enhance access to knowledge. In parallel, Armenia should develop a national framework to allow for systemic collection and analysis of data on SME skills, and use the insights gathered to develop new training programmes and inform policymaking. Finally, monitoring and evaluation practices could be improved by ensuring the assessment of the concrete impact of each of the training initiatives. Establishing an impact monitoring framework for SME training would ensure the high quality and efficiency of implemented capacity-building services, while the good training practices identified could then feed into new programmes.

## *Pillar C: Access to finance*

### *Legal and regulatory framework*

Armenia has a reasonably well-developed legal framework for bank lending. A functioning cadastre and register for movable assets are in place and according to a recent bank survey conducted by the EBRD, around half of Armenian banks think that the framework works well – although enforcement needs to be strengthened, with a quarter of banks thinking enforcement of security rights over immovable assets is too cumbersome, and 46% of banks thinking the same when it comes to movable assets (EBRD, 2021[29]). Consequently, banks tend to not rely on movable assets for their credit decisions toward SME customers. Credit information is collected from banks, non-financial institutions and utilities, allowing a wider range of the population to build up a credit history.

The Central Bank of Armenia has strengthened its supervisory toolkit by further aligning its regulatory framework with the Basel III principles and improving its risk-based supervision framework that was first adopted in 2017 (IMF, 2022[4]). Past measures to encourage local currency lending seem to have taken hold, as dollarization in the country has reduced: around 40% of corporate lending by banks and credit organisations was in local currency in June 2023 compared to 22.7% in June 2019, at the time of the last SBA assessment. At the moment, ESG reporting is not yet required, meaning that banks have no non-financial disclosure requirements; consequently, no green taxonomy is in place yet, although one is under development.

Capital markets are regulated under the Law on Securities Market, the Law on Investment Funds and a number of other relevant regulations. In 2020, a new capital markets development strategy was approved and is currently under implementation. The Armenia Securities Exchange is the local stock market which is regulated by the Central Bank of Armenia. Key activities are listing and trading of stocks and bonds, with 28 active issuers and close to 100 traded bonds, as of September 2023. This means that the market is relatively small, and listings consist primarily of banks and a number of local corporates. Equally, 82% of corporate bonds issued are by local banks. The exchange therefore does not seem to constitute a realistic funding option for medium-sized or smaller companies. However, the Ministry of Economy submitted a proposal to support bond issuers with transaction costs and the acquisition of a rating from a rating agency, which was approved in June 2023. These measures could help encourage more issuances.

### *Sources of external finance for SMEs (bank financing, non-banking financing, and venture capital)*

Credit to corporates and SMEs in absolute terms has remained relatively stable since December 2019, and while GDP in current prices dipped in 2020 due to the pandemic, it has grown since then (IMF, 2021[30]). This suggests a gap between the financial sector and the real economy. It would be important to bridge this gap in order to turn the financial sector into a pillar that supports economic growth going forward.

Indeed, improving access to finance is one of four pillars of the country's SME Development Strategy 2020-2024 which aims to facilitate SME growth and productivity and is also reflected in the Government of Armenia's 5-year programme 2021-26. Activities to date have focused on improving access to finance for start-ups and growth companies, non-bank financing mechanisms such as leasing and crowdfunding, and the development of capital markets.

When it comes to SMEs' perception of their ability to access financing, Armenia has one of the highest shares of firms thinking that access to finance is a major or very severe obstacle to doing business. According to a recent enterprise survey, around 35% of SMEs indicate a lack of external funding sources to be a major issue (the only country in the region with a higher share, 46%, is Ukraine). Around 32% of SMEs who are credit constrained (i.e. they need a loan but cannot access one) report that they did not take out a loan because of unfavourable interest rates, suggesting that there is a clear issue of affordability (EBRD, 2021[31]).

The recent re-organisation of the institutional structure through which SME support is provided means that Enterprise Armenia is likely to take on most of the responsibilities that resided with the SME DNC before (others now sit with the Ministry of Economy directly). The restructuring has also triggered a more in-depth review of existing funding programmes, including the credit guarantee scheme (supported by the EU and World Bank). During the COVID pandemic, the credit guarantee scheme was propped up to provide guarantees of around AMD 1 billion (EUR ~2.36 mln), a significant increase compared to previous levels. The scheme currently has little private sector involvement and is entirely reliant on government funding – two aspects that should be reviewed as part of its general overhaul. In addition, while regular monitoring of results by the Ministry of Economy is carried out, no evaluations or impact assessments seem to be carried out. This is a major shortcoming as such more in-depth assessments are crucial to assess the workings of the programme and its impact on financial inclusion. The same applies to other access to finance support programmes, including the interest rate subsidy provided by the Economic Modernisation Program. Results from such evaluations should also be shared with various stakeholders (including private banks and business associations) in order to create the opportunity for a feedback loop around programme design. This is extremely important in order to determine whether programmes are effective in reaching their policy goals.

The Ministry of Economy has also launched an Economic Modernisation Program which provides interest rate subsidies on loans and leases for the purchase of modern (new) equipment and machinery. The total budget of the programme for 2023 is AMD 8.2 billion (EUR ~19.4 mln). The subsidy rate ranges between 6% and 10%, depending on the instrument and currency (leasing instruments and local currency funding attracts a higher interest rate subsidy) (Ministry of Economy of Armenia, n.d.[32]). The programme has certain caps in place, for instance, on duration and amount of the subsidy, but it does not limit repeated use, which could constrain its potential to reach new beneficiaries. Including both loans and leasing products in the programme is a good way to encourage leasing activities rather than solely focusing on bank credit. Financial support is also available through several programmes managed by the German-Armenian Fund (GAF). Some programmes funded by international financial institutions (IFIs) are also managed through the GAF, targeting female-owned or managed enterprises as well as firms active in agriculture and tourism.

Access to non-bank financing has improved since the last assessment when it comes to leasing and venture capital (VC). However, microfinance volumes have steadily dropped by 30% since 2019 (Central Bank of Armenia, n.d.[33]). Microfinance is mainly provided through credit organisations that are regulated by the Central Bank of Armenia. They are not allowed to raise deposits, somewhat limiting their role within the financial system. The legal framework for leasing and factoring is based on the Civil Code, which stipulates that these services can only be provided by a bank or licensed entity. While factoring volumes have been stable since the last assessment, leasing transactions have seen a more than five-fold increase between 2019 and 2022. The uptake of leasing as a financing instrument is further supported by the

Economic Modernization Program discussed above. A similar approach to support factoring is under discussion.

Private equity could be further developed, but given the size of the market, there are a reasonable number of equity and VC funds active in the country. One example is the EU-Armenia SME Fund managed by Amber Capital, which aims to support SMEs with growth potential. It is supported by a range of IFIs and private and institutional investors, including the EU and EBRD, as well as the Armenian government (via the Armenian National Interests Fund). More generally, Armenia's government has made efforts to develop the VC sector and tap into the Armenian diaspora for investments. In 2013, Armenia's first venture fund, Granatus Ventures, was launched with government participation to invest in start-ups in the tech sector. Since then, the fund's portfolio has grown substantially, and a number of successful exits have been completed. In 2019, a second fund, Granatus Tech4SDG, was launched with support by UNDP to invest in tech start-ups with a strong potential for ESG impact. There are also a number of private VCs operating in the country, many of which focus on earlier stages of development. To build on positive past experience, a proposal for a fund of funds supported by the government is currently under consideration. Business angels can connect and exchange through the Business Angel Network of Armenia (BANA), which brings together local investors as well as Armenians living abroad. Finally, the Central Bank adopted new regulation on investment-based crowdfunding in February 2022 to facilitate the offering of crowdfunding platforms in the country.[5]

### *Financial literacy*

The latest Financial Capability Survey was conducted in 2019. The results suggest that fewer than half of Armenians have an adequate understanding of financial concepts. In response, the National Financial Literacy Strategy for 2021-2025 focuses on improving personal and household level financial literacy in the population. To help raise financial awareness, the Central Bank of Armenia has launched two online platforms. One of them is abcfinance.com which explains financial concepts, provides guidance on how to go about making certain financial decisions (e.g., how to plan for retirement, manage debt, types of payments etc.), and provides practical tools, for example, on budgeting. It also contains educational material aimed at younger people as well as teachers. The second platform, fininfo.am, provides information about financial instruments and allows potential borrowers to compare products. These are all important steps and tools to improve the understanding of financial concepts among the population. Both the strategy and platform primarily target the general population, however, and only offer limited resources targeted at small business owners.

### *Digital financial services*

No formal strategy for digital financial services has been developed, but it is a pillar in the Central Bank's general development strategy. The leading authority dealing with issues in this field is the Central Bank of Armenia whose Financial Stability and Regulation Directorate deals with policy and regulatory approaches to digital financial service provision. The regulatory framework surrounding digital finance is still under a relatively early stage of development. Data protection is currently covered by general regulation but plans exist to regulate the use and protection of data in the context of digital finance specifically, and to move toward an open finance framework in which data sharing obligations and their modalities will be defined. More sophisticated regulatory tools such as supervisory technology ("suptech"), regulatory sandboxes, and a Central Bank digital currency are not in place yet, but are under development.

### *The way forward*

Access to credit for SMEs could be strengthened by improving the legal framework for secured transactions. When it comes to taking security, the use of movable assets as collateral should be made easier. Banks clearly do not see this as a viable option. Following an analysis to determine why this might

be the case, necessary steps should be taken to remedy this issue. Furthermore, enforcement processes will need to be streamlined and made more efficient to encourage bank lending to SMEs. Even if the definition and registration of collateral worked well, the lack of an efficient enforcement mechanism will be a major drag on bank lending as commercial banks need to spend significant resources to protect themselves in the case of borrower defaults.

Introducing ESG reporting requirements would improve the overall regulatory framework by allowing the monitoring of a wider range of parameters that are increasing in importance. In this context, it is important to set out clear standards for reporting so that banks are able to follow straightforward rules when it comes to the analysis of their portfolios. In this context, finalising the development of a green taxonomy will be crucial to move forward on this front.

As noted during the previous SBA assessment, evaluation mechanisms for financial support programmes, be it grants or guarantees, need to be strengthened. It is good that a more comprehensive review of support programmes has been carried out and that some of them are being redesigned as a result. However, this was more of an ad hoc measure, rather than being part of a systematic review mechanism. Currently, basic metrics around programme implementation are being collected (number of beneficiaries, etc.), but there is no systematic review of the economic impact of state support – i.e. the extent to which these programmes achieve their stated policy goals, such as improved access to finance, increased financial inclusion, or higher investment activity.

The Armenian government has made progress when it comes to supporting leasing and venture capital, but factoring is not widespread. It would be useful to conduct an analysis of why this instrument is little used (e.g. gaps in the legal framework, low awareness). This should also include considerations for reverse factoring which can be valuable for SMEs to access cheaper working capital finance within a supply chain.

When it comes to digital finance, projects currently under development should be moved forward in order to have a more comprehensive and sophisticated regulatory framework for digital financial services. While the Central Bank is a natural leading institution, care should be taken to have an institutionalised multi-disciplinary approach – because digital finance in particular is an area where insights from other disciplines and institutions can play an important role (e.g., consumer protection, competition, ICT regulation, data protection).

Finally, expanding information sources and financial education awareness-raising campaigns to target entrepreneurs specifically would be helpful to provide SME owners and managers with the necessary skills to improve their accounting and business planning and enable them to take advantage of different financing products. Adding entrepreneurship specific components to existing tools (financial literacy survey, training) will go a long way in catering for business owners' needs. In addition, an online platform with explanations of different business relevant financial products and information about their availability can help close information gaps. Having a credible and reliable platform can go a long way in supporting the diversification of funding sources, by raising awareness of small business owners who tend to have fewer resources to shop around. This could be done through a new portal or added to existing resources, such as the information website abcfinance.am. In addition, consideration could be given to more stringent reporting and auditing requirements for SMEs at the larger end of the definition in order to improve financial accounting capabilities and access to finance.

## *Pillar D: Access to markets*

### *Public Procurement*

The situation in the field of public procurement remains largely unchanged since the latest assessment, apart from a new set-up for handling complaints and adjustment of some details in the legal and institutional framework and the e-procurement system.

Armenia has been a party to the WTO's Government Procurement Agreement since 2011 and is thus obliged to abide by its provisions. At the same time, its public procurement policies and practices must also reflect Armenia's commitments as a member of the Eurasian Economic Union, potentially leading to legal uncertainty. Public procurement remains regulated by the Public Procurement Law (PPL) of 16 December 2016, with few recent amendments, and by corresponding government decrees and other pieces of secondary legislation. The full implementation of the principles and provisions of the PPL would merit continued attention but, at present, there is no strategy or policy for further developing public procurement. The current SME development strategy contains several objectives for developing SME participation in public procurement, but corresponding mechanisms are not yet fully in place.

A Ministry of Finance department is the authorised body in charge of regulation and co-ordination of public procurement and operates the e-procurement system. The use of the latter is mandatory, and electronic auctions must be used for a specific list of items, determined by the government. The review body formerly in charge of handling complaints against public procurement decisions taken by the contracting authorities was dissolved in 2022, and complaints must now be lodged with the courts. However, it is not yet evident if these are able to handle complaints with the competence and speed expected.

The e-procurement system allows information to be extracted about the various steps carried out using the system. However, the total value of reported public procurement as a percentage of GDP appears to be significantly lower than in comparable countries, indicating a possible information gap. Data on SME participation in public procurement is not systematically collected or otherwise easily accessible, and there is no obligation to publish evaluation reports or contracts for small value procurement (below AMD 1 mln, or EUR ~2 400).

Some regulatory features, such as the possibility of division into lots and an obligation of rapid payment of invoices, have the potential to facilitate SME participation. Other features are likely to have the opposite effect: for example, a tender security is often required and there is no longer any ceiling amount for this. However, because of the lack of data, it is not possible to evaluate the effects, whether positive or negative, of the various features of regulations and practices affecting SME participation.

Various standard documents and guidelines are published and can be accessed through the e-procurement system, allowing SMEs to research available business opportunities as well as the procurement procedures to be followed. However, there is no training on offer specifically for SMEs, nor on how contracting authorities can facilitate SME participation. The earlier requirement involving examinations for public procurement officials has been abolished, but the need to raise their professional skills remains. The PPL still foresees the use of ad hoc tender committees rather than dedicated, full-time professionals with appropriate training, administrative resources and management support. The latter would be more effective in enhancing the potential of well-managed SMEs to provide better value for money in public procurement.

Improving the scope for better SME participation would thus require meeting several challenges, notably i) setting public procurement in a wider, medium-term strategic context and revising the PPL and applicable regulations to further facilitate SME participation; ii) improving the collection and evaluation of public procurement data, including data on SME participation, in order to create a more solid evidence base; and iii) raising the level of professionalisation by reorganising the public procurement function within contracting authorities and improving the skills needed to plan, prepare, award, and manage contracts.

### *Standards and Technical Regulations*

There have been various developments in the field of standards and technical regulations. Armenia's harmonisation with the EU acquis faces particular challenges in this context as the country seeks to effectively combine the benefits of participating in the two different trading blocks of the Eurasian Economic Union and the European Union.

In terms of overall co-ordination and general measures, several consolidations have taken place. In 2019, the national institutes of standards and metrology were modernized and transformed into the National Body for Standards and Metrology (ARMSTANDARD) under the responsibility of the Armenian Ministry of Economy (ISO, n.d.[34]). Armenia has developed annual state standardisation programmes since 2020, a programme on the development of metrology, and a list of measures for 2020-23. To strengthen Armenian stakeholders' competencies in the field of quality infrastructure, ARMSTANDARD also has a training centre that offers courses in standardisation, metrology and conformity assessment (ISO, n.d.[34]).

A specific challenge is the international recognition of the accreditation system, mainly because Armenia is not a member of the International Laboratory Accreditation Cooperation (ILAC) or the International Accreditation Forum (IAF) and is only an associate member of the European co-operation for Accreditation (EA). To address this limited recognition, an application for EA Multilateral Agreement (EA-MLA) signature status is being prepared as a first step. Other action items are the still-limited availability of domestic conformity assessment services, the development of the country's market surveillance system, and the further development of the quality infrastructure's regular evaluation.

Concerning harmonisation with the EU *acquis*, Armenia has implemented a roadmap for transposing EU sectoral legislation in priority sectors. A proposal to bring Armenia's legislation on accreditation into line with the EU *acquis* has also been prepared. Other actions to be taken include aligning legislation on conformity assessment with the EU acquis and securing recognition of ARMSTANDARD by relevant international and European metrology organisations. The adoption of European Standards (EN) continues, with 50% of standards adopted so far – making further adoption also an important measure in the following years.

Addressing the goal of providing SMEs with Access to Standardisation, ARMSTANDARD provides specific financial conditions for acquiring standards for SMEs. Between 2018 and 2021, almost 30 SMEs received annual financial support to improve their access to standardisation. Armenia also has a working group that assesses SMEs' needs and concerns and provides appropriate services and information. A recent example of SMEs' involvement in standardisation was the formulation of requirements on berries in a fruit product; this practice should be replicated in other areas. Another action item is developing measures to facilitate SMEs' access to conformity assessment.

Regarding the digitalisation of standards and technical regulations, Armenia has a strategy to ensure the digital transformation of the government, economy and society. The Armenian Ministry of High-Tech Industry has also developed a digitalisation toolkit to be adopted by the country's technical regulators. An action item is to ensure that there are designated staff or special working groups for digitalisation.

### *Internationalisation of SMEs*

Armenia has made limited progress in the area of SME internationalisation.

The country’s performance in export promotion has been hindered by the major changes that the institutional framework for SME support has undergone since the last assessment. Although the newly adopted SME Development Strategy 2020-2024 defines the promotion of SME exports as one of its key objectives, the Export-led Industrial Development Strategy adopted in 2011 remains the main strategic document guiding policy developments in this area. Although the Ministry of Economy has always been responsible for SME policy in the country, the SME DNC – the agency in charge of implementation – was recently liquidated. Its mandate was transferred to two government bodies: the Investment Support Centre, a government agency operating under the brand “Enterprise Armenia”; and the Department of Entrepreneurship within the Ministry of Economy, which is now responsible for both policymaking and implementation of support programmes, including the Investment and Export Promotion Programme. Within this programme, the Ministry provides a variety of promotion activities, such as facilitation of trade missions, SME participation in trade fairs, information support and consultancy services.

At the same time, Enterprise Armenia, within the framework of the Enterprise Europe Network (EEN), provides information services to SMEs that are interested in export or co-operation with international suppliers. Finally, the Export Insurance Agency of Armenia (EIAA), a state-owned institution operating within the Ministry of Economy, provides exporters with insurance against non-payment and helps secure funding from financial institutions on preferential terms. In 2020, the sum insured by the EIAA comprised over 1.5% of overall exports, with 32 companies benefiting from its services. This is, however, the only form of financial support that SMEs receive for export promotion.

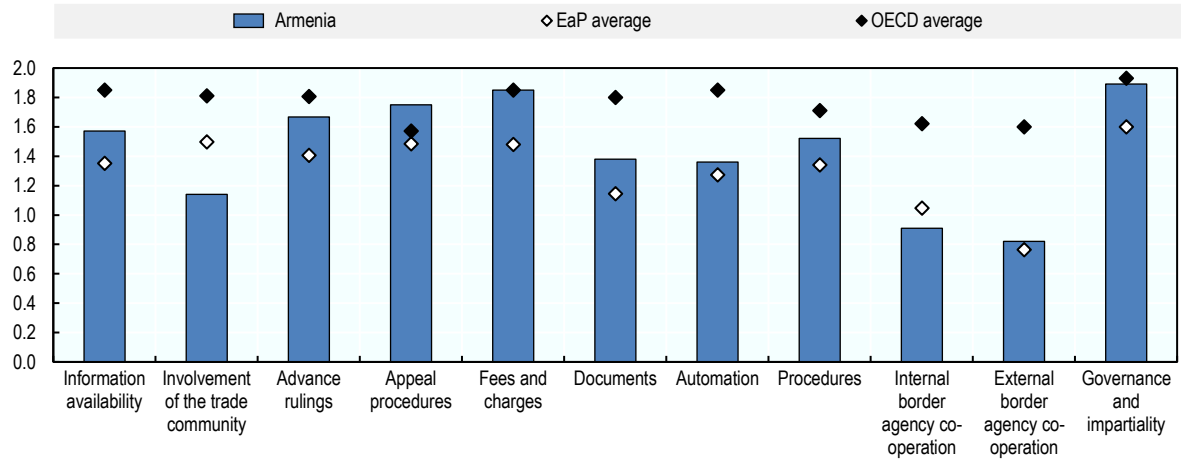
The regulatory framework for e-commerce in Armenia is rather comprehensive, as it covers most relevant aspects, including e-signatures, e-payments, and consumer and data protection. “Economic modernisation and increased competitiveness through digital platforms and smart solutions” is one of the three main directions of the Digitalisation Strategy of Armenia for 2021-2025, and a number of measures targeting the promotion of e-commerce are also suggested in the SME Development Strategy for 2020-2024, which includes as one of its priority actions “Creation of a favourable environment for the expansion of e-commerce”. These measures include activities such as i) the launch of an electronic certificate-of-origin system, enabling access to international online payment systems; ii) a study of the payment systems and postal services and, if necessary, the development of an agenda for institutional and legislative reforms; iii) the development of guidelines in the form of a manual containing information on all stages of product sales on global and regional electronic platforms, as well as electronic sales; and iv) the provision of technical support for e-commerce.[6] However, since the unprecedented crisis of the COVID-19 pandemic in 2020, the implementation of these measures has faced significant challenges.

The government's action plan for 2021-26 sets “Development of electronic commerce” as one of its goals. In this regard, a draft law "On Electronic Commerce" is expected to be presented to the government. Furthermore, it is worth mentioning that an e-commerce pilot programme between Armenia, Azerbaijan, Georgia and Germany was launched in 2021 by EU4Digital to establish national virtual warehouses/databases of local goods to connect e-commerce actors so that they can automatically exchange information about sales, customs and delivery (EU4Digital, 2021[35]).

Armenia does not provide evident support to promote SMEs’ integration into global value chains (GVCs). Although there seems to be a proposal for the introduction of a government programme on this subject, there is no available information in this regard.

Nevertheless, the country’s performance in the 2022 OECD Trade Facilitation Indicators has strongly improved since 2017,[7] and Armenia now outperforms the EaP average in almost all areas assessed. Performance has improved since 2019 in simplification and harmonisation of documents, streamlining of procedures, and internal and external border agency co-operation. Nonetheless, the government should direct efforts towards improving the percentage of advance rulings issued within the announced average time period, and further expanding the acceptance of copies of documents and the use of the Authorised Operators programme.

## Figure 10.5. OECD Trade Facilitation Indicators for Armenia (2022)




Note: The Trade Facilitation Indicators (TFIs) take values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade Facilitation Indicators Database, https://oe.cd/tfi.

StatLink https://stat.link/75x4le

Moving forward, in order to facilitate integration into GVCs, the government could consider i) introducing support programmes aimed at promoting cluster development and ii) fostering business linkages through measures such as matchmaking and incentives for FDIs (e.g. tax credits to foreign-invested firms that provide tangible benefits to domestic suppliers). Moreover, to enhance the effectiveness and accountability of existing programmes supporting SMEs' access to international markets, the government could establish a comprehensive system for monitoring and evaluation, which is currently lacking across all sub-dimensions.

### *Pillar E: Innovation and business support*

#### *Support services for SMEs and start-ups*

Armenia's institutional arrangements for SME support services have experienced important changes in the last four years. The SME DNC, the governmental agency delivering a wide range of financial and non-financial support services to since 2002, has been closed and its functions transferred to the Department of Entrepreneurship within the Ministry of Economy and to a separate agency, the Investment Support Centre, operating under the brand "Enterprise Armenia", whose mandate also includes investment promotion.

This transition has had the net effect of reducing the government's overall capacity to assist the SME population. Since 2022, SME support programmes have comprised only a small part of Enterprise Armenia's operations, as the agency implements small-scale programmes to provide basic training, consulting services and support for business internationalisation to start-ups and SMEs. Furthermore, feedback received from the private sector highlights how the closing down of the SME DNC's network of local offices throughout the country has reduced the government's ability to reach out to SMEs in the regions, both to increase awareness about available support programmes and to listen to the needs of entrepreneurs outside the capital city, which had previously been an important tool for developing an inclusive SME policy.

Support programmes for start-ups are now administered directly by the newly established Ministry of High-Tech Industry. A range of mostly donor-led and public-private initiatives complement the offer of available

services for start-ups through incubation facilities and acceleration programmes, such as the Enterprise Incubator Foundation and the ImpactAIM initiative.[8]

Although government plans to support SME digitalisation are gaining momentum, structured programmes in this area are still missing from the set of publicly sponsored initiatives available to SMEs. Commendable steps have been taken in the preparatory phase, for instance through the "Draft action plan for the digital transformation of the manufacturing and services sectors", which presents detailed targets and a precise indication of the financial resources required, although its approval is still pending. The main challenge moving forward will be to identify a strong co-ordinating institution with the mandate and resources to translate strategic priorities into concrete initiatives supporting the digital transformation of SMEs. In doing so, such entity could leverage existing donor-led initiatives (e.g. EBRD-trained consultants advising SMEs on their digital transformation) and a dynamic ecosystem of non-governmental actors active in the development of digital skills and digital entrepreneurship (e.g. the Armath Engineering Laboratories, the TUMO Centre for Creative Technologies, and the Gyumri Technology Centre – see Box 4.2 in the "Digital Economy for SMEs chapter").

Lastly, it is worth mentioning Armenia's initial efforts to collect internationally comparable statistics on the adoption of digital technologies in the business sector. In 2023, Armstat carried out a pilot survey of 2 400 firms following Eurostat's model for ICT Usage in Enterprises.[9] This is a very positive development towards expanding the set of outcome-oriented indicators for digitalisation policies in Armenia, provided that such data become a regular output of the national statistical production.

Moving forward, the government should identify a co-ordinating agency with a strong mandate to design and deliver services for SMEs, including a dedicated programme of SME digitalisation. The focus on technology and start-ups in the IT sector should be complemented by initiatives aimed at increasing diffusion of digitalisation in other sectors of the economy. In doing so, it will be important for the new agency to leverage the existing ecosystem of external advisors when providing support services for SMEs. Lastly, Armenia could build on the pilot survey to integrate ICT use by businesses as a regular statistical output of Armstat.

### *Innovation policy for SMEs*

The policy framework for innovation in Armenia has not seen significant changes since the previous SBA assessment. While no national strategy for innovation is currently in place, elements of innovation policy and support for innovative SMEs can be found in other strategic documents, including the SME Development Strategy 2020-2024 and the Government Program 2021-2026. In this regard, a new innovation strategy is being developed, which is expected to define the government's vision, clarify institutional responsibility for promoting innovation in the country, and improve overall policy coherence.

On the institutional side, Armenia also lacks a dedicated agency with a broad mandate to implement innovation policy. Responsibilities for the design, implementation and monitoring of innovation policies are broadly split between the recently established Ministry of High-Tech Industry (in ICT and high-tech sectors), the Ministry of Economy (in "traditional" sectors, such as agriculture and manufacturing) and the Science Committee within the Ministry of Education, Science, Culture and Sports (promoting innovation in the science and academic sectors). Overall, government support for SME innovation is available through isolated initiatives, mostly aimed at the IT sector and implemented by unco-ordinated actors. In addition, the National Academy of Sciences hosts 31 research institutes and carries out research across five fields: mathematical and technical sciences, physics and astrophysics, natural sciences, chemistry and earth sciences, and social sciences.

Incubators, accelerators and science and technology parks feature in Armenia's innovation support infrastructure. However, most of the activities are implemented with donor funding and remain focused on assisting early-stage IT start-ups through training, mentorship and networking programmes. The Enterprise Incubator Foundation (EIF) continues to be the primary player in the start-up ecosystem, managing

projects such as the Gyumri and Vanadzor Technological Centres and the Engineering City, a science and technology park with research and prototyping laboratories for companies in the electronics and material science sectors.

Governmental support for technology transfer in Armenia remains limited, which is mostly due to institutional and regulatory gaps. The National Centre for Innovation and Entrepreneurship, a body operating under the Ministry of Economy, has recently been tasked with promoting technology transfer in the country; however, the agency appears to lack the human and financial resources needed to take on this role. The only initiative supporting technology commercialization and science-business collaboration is the Science Incubation Program, implemented by EIF and the PMI Science R&D Center.

In the last four years, the government has introduced important tools providing financial support for innovation. Initiated in 2020, the flagship programme of the MoHTI, “From Idea to Business”, offers financial and incubation services to start-up technology companies and research teams to develop and commercialize their ideas. In particular, grant competitions provide start-ups with funding at the idea (up to AMD 5 million / ~ EUR 11 000) and growth stages (up to AMD 10 million / ~ EUR 22 000) to facilitate product development and market entry. In addition, in January 2022 the government approved a new set of incentives to modernise the economy (Government Resolution 106-L). Through this programme, eligible Armenian entrepreneurs can benefit from subsidised interest rates for loan and leasing agreements contracted to purchase new machinery and equipment. This package has been very well received by the community of Armenian entrepreneurs, with nearly 1 000 credit and leasing agreements signed in the first nine months of the programme and manufacturing companies reportedly starting to export thanks to the increased quality of their production.

Moving forward, the government could consider improving overall policy coherence and channelling its diverse set of innovation support measures into one comprehensive national strategy. Monitoring and evaluation practices could also improve, moving beyond simple programme implementation (e.g. tracking disbursement of funds) and looking specifically at the lasting impact of financial support tools on innovation performance in the business sector.

### *SMEs in a green economy*

Armenia’s policy framework continues to lack a dedicated approach for promoting green practices among SMEs, although elements of such environmental policies can be found in the SME Development Strategy 2020-2024 and the Program on Energy Saving and Renewable Energy for 2022-2030. While only one reference to promoting tools to support green technologies appears in the former, the latter reflects energy saving and energy efficiency improvement measures in selected sectors, including industry and agriculture, which are dominated by SMEs. The programme is supported by an action plan for implementation, measurable targets, and expected impact.

Armenian SMEs do not fully appreciate the benefits of managing the environmental side of their businesses, resulting in low adoption rates of environmental management systems. Barriers to implementation include a lack of information, capacity, and the perceived high cost and time burden required. Although training courses are available, they are expensive and not targeted towards SMEs. While guidance for SMEs on greening practices and financing options is offered by the Ministry of Environment, Ministry of Energy, and Ministry of Territorial Administration and Infrastructure, a dedicated agency for SME support in this area would be more effective.

Dedicated government incentives to support SME greening in Armenia are not widely available, although the Renewable Resources and Energy Efficiency (R2E2) Fund plays an important role in financing renewable energy projects. On the other hand, financing options for SME greening projects, mostly donor-funded, have started to appear, and include the EBRD-led “Finance and Technology Transfer Centre for Climate Change” (FINTECC) initiative, which helps businesses adopt climate technologies for renewable energy and resource efficiency, and the EU-financed “Promoting Green Lending in the Eastern

Partnership" project, which channels green financing to SMEs through local commercial banks. Furthermore, the government plans to introduce green bonds as well as tax incentive-based instruments to reduce pollution and resource use as part of the Nationally Determined Contribution Financing Strategy and Investment Plan, which is not yet approved. However, data on the impact of regulatory or financial incentives on SME greening are not available, and there is a need to develop the taxonomy and capacity for monitoring and evaluating sustainable finance initiatives (e.g. green bonds).

## Way forward

To further improve its SME policy, the Armenian government should consider the following measures:

- Armenia's adoption of the DSA is a very welcome step; however, the government should closely monitor its implementation, clarify stakeholder roles, and ensure consistent funding. Enhanced co-ordination and data collection on digital transformation are crucial for policy impact assessment and could be significantly improved, e.g. by using the OECD Going Digital Framework as a reference. To boost broadband uptake, Armenia should improve Internet affordability, enhance data collection for accurate assessments, and conduct multi-stakeholder consultations for the broadband strategy. Armenia benefits from a range of initiatives to foster digital skills development, largely led by the private sector. This approach could be complemented by enhanced co-ordination, awareness-raising, and monitoring and evaluation of the solutions available. More could also be done with regards to skills assessment and anticipation tools, as well as support targeted at SMEs.
- To revitalise SME development, Armenia should strengthen institutional capacity, allocate more resources, offer a well-defined mandate to stakeholders, and re-establish regional offices to provide local support. Additionally, Armenia should address the informal sector with measures to improve tax compliance, accelerate regulatory reforms and enhance RIA application to streamline processes. Building on its efforts to improve the operational environment for SMEs, Armenia should expand e-government services, focusing on promoting e-commerce and digital transformation at the enterprise level, and regularly review and update licensed activities to ensure public safety and ease of doing business. Armenia's bankruptcy proceedings for legal and natural persons can be further improved to reach international standards. This includes streamlining bankruptcy procedures and introducing out-of-court debt restructuring options to reduce costs, as well as implementing pre-insolvency tools like public awareness campaigns, advisory services, and early-warning systems that would assist entrepreneurs in financial distress. A dedicated policy to promote a second chance for bankrupt entrepreneurs seeking a fresh start, including the removal of barriers to re-enter the market, should be implemented. Monitoring and evaluation practices need to be developed to increase the efficiency and effectiveness of bankruptcy and prevention policy.
- To bolster entrepreneurial learning, Armenia could further enhance pre-service and in-service teacher training on entrepreneurship, and foster cooperation between general secondary schools and SMEs. Additional efforts could be made to monitor and evaluate learning outcomes and track graduates, to gauge the effectiveness of educational initiatives. With regard to women's entrepreneurship, the policy approach would benefit from more co-ordination and data insights – e.g. through monitoring and evaluation, enhanced data collection and the conduction of regular surveys on barriers to women's entrepreneurship. Addressing persisting issues like informality will formalise businesses and create a conducive environment, while gender sensitivity checks in policies will promote inclusivity and gender equality. Implementing an impact monitoring framework for SME training can ensure effective delivery of high-quality capacity-building services, promoting continuous improvement and best practices. In the realm of SME training and awareness, Armenia should improve co-ordination among support providers and donors to maximize the impact of programs. A single online portal can raise awareness of available training opportunities.

Developing a national framework for data collection will inform policymaking and enable targeted training programs.

- To improve SMEs' access to finance, Armenia should consider introducing ESG reporting requirements as well as further improving the legal framework for secured transactions by facilitating the use of movable assets as a collateral and streamlining and strengthening enforcement processes. Additionally, evaluation mechanisms for financial support programmes need to be strengthened. Armenia should also analyse challenges to financial factoring uptake, including considerations on reverse factoring. Furthermore, adopting a more comprehensive and sophisticated regulatory framework that institutionalises a multidisciplinary approach to digital finance will be crucial. Finally, expanding information sources and financial education awareness-raising campaigns to target entrepreneurs specifically is key to enable entrepreneurs to take advantage of the existing financing products.
- Armenia can enhance SME participation in public procurement by revising the Public Procurement Law and regulations to facilitate SME involvement and taking measures to ensure that all such provisions are properly applied. Improving data collection and evaluation on SME participation is crucial, together with raising the level of professionalisation in the procurement process and improving the skills of professionals involved in planning, preparing, awarding, and managing contracts. Despite progress in standards and technical regulations, Armenia continues to encounter difficulties in harmonising with both the EEU and the EU. To overcome these challenges, Armenia should focus on obtaining international accreditation recognition, aligning its legislation with the EU acquis, and increasing the adoption of EN standards. Supporting SMEs via improved access to standardisation and conformity assessment is essential. Moreover, prioritising government, economy, and societal digitalisation by adopting a digital toolkit for technical regulators will significantly enhance progress. To promote integration into GVCs, Armenia should introduce support programs for cluster development and business linkages, including matchmaking and incentives for FDIs. Establishing a comprehensive monitoring and evaluation system will allow for improving the effectiveness of programmes supporting SMEs' access to international markets.
- To support services for SMEs and start-ups, the Armenian government should establish a co-ordinating agency for designing and delivering services, leveraging external advisors and the broader ecosystem of support service providers, especially to promote SMEs' digital transformation. The government should also focus on improving policy coherence and consolidating innovation support measures into a comprehensive national strategy. To promote green practices among SMEs, Armenia should develop a comprehensive strategy, including affordable training courses on environment management systems. A dedicated agency can also enhance support for greening practices, while introducing dedicated tax incentives and financing options. Implementing effective monitoring and evaluation mechanisms is crucial for assessing the impact of financial tools on innovation, as well as ensuring the effectiveness of support services, innovation and greening initiatives.

### Table 10.5. Roadmap for policy reforms – Armenia

| **Strengthening framework conditions for the digital transformation** |
|---|
| • Monitor DSA implementation, define and enhance co-ordination with stakeholders, and secure continuous funding. |
| • Collect additional data on the digital transformation to assess policy impact. |
| • Encourage broadband uptake by improving Internet affordability, especially for fixed broadband. |
| • Enhance data collection to better assess digital divides. |
| • Offer reliable data on subscriptions, coverage, and quality to empower consumers and incentivise network improvement. |
| • Seek multi-stakeholder consultations for the upcoming broadband strategy's development and implementation. |
| • Foster collaboration and co-ordination between public and private initiatives, enhance awareness, and monitor stakeholder impact. |
| • Improve digital skills assessment and tools by collecting data and adopting a digital competence framework in line with DigComp. |

- Promote digital skills development among businesses to address the lack of digital literacy hindering SME digitalisation.

**Enhancing the institutional and regulatory framework and operational environment for SMEs**

- Revise SME Strategy to align with post-COVID recovery and economic shifts, e.g. IT sector growth.
- Identify strong co-ordinating agency or unit in charge of implementing SME policies
- Ensure SMEs outside the capital city can access services via updated local development strategy.
- Apply RIA broadly, including SME test, to pertinent laws.
- Review and enhance e-government services to ensure quality provision for SMEs.
- Strengthen co-ordination among public entities, focusing on areas like business licenses and tax compliance.
- Collect SMEs' e-government usage data, promote service adoption through digital skills improvement and campaigns.
- Analyse SME tax rates, prevent distortions from tax incentives, and encourage accurate reporting.
- Enhance bankruptcy procedures with out-of-court debt restructuring.
- Introduce pre-insolvency tools for entrepreneurs in financial distress.
- Introduce policies to support bankrupt entrepreneurs and remove market re-entry barriers.
- Develop monitoring and evaluation practices for bankruptcy and prevention policy.

**Promoting entrepreneurial skills and women entrepreneurship development**

- Enhance entrepreneurial learning via mandatory pre-service teacher training and in-service training in VET institutions.
- Foster co-operation between general secondary schools and SMEs to promote entrepreneurial learning at all education levels.
- Improve monitoring and evaluation of graduates' progress in entrepreneurial learning.
- Enhance co-ordination among public and private stakeholders to assess women entrepreneurs' needs and monitor policy impact.
- Conduct regular surveys on barriers to women's entrepreneurship to gain insights into challenges and develop support measures.
- Establish an impact monitoring framework for SME training to ensure high-quality and efficient capacity-building services.
- Co-ordinate public-private efforts for effective needs assessment and policy impact monitoring for women entrepreneurs.
- Resolve concerns as informal support for women's entrepreneurship, formalising businesses and creating a supportive environment.
- Conduct gender sensitivity checks for policies to ensure inclusive and gender-equal support for women entrepreneurs.
- Increase co-ordination among business support service providers and donors to avoid overlaps and maximise impact.
- Raise awareness of available training opportunities for SMEs via a single online portal.
- Develop a national framework for collecting and analysing data on SME skills to inform policymaking and develop new trainings.

**Facilitating SME access to finance**

- Ease the use of movable assets as collateral when taking a security.
- Encourage bank lending to SMEs by streamlining of enforcement processes and enhancing their efficiency.
- Strengthen evaluation mechanisms for financial support programmes via the systemization of reviews.
- Introduce ESG reporting requirements to monitor more parameters that are gaining in importance.
- Conduct an analysis on challenges to financial factoring and consider reverse factoring to help SMEs access cheaper working capital finance.
- Develop a more comprehensive, sophisticated, and multidisciplinary regulatory framework for digital financial services.
- Expand targeted information sources and financial education awareness-raising campaigns for entrepreneurs.

**Supporting SME access to markets**

- Set a wider, medium-term strategic context and revise the Public Procurement Law and regulations.
- Improve data collection and evaluation, including SME participation, for a stronger evidence base.
- Raise professionalization via reorganization and skill improvement in contracting authorities.
- Strengthen competencies in quality infrastructure via training services and state standardization programmes.
- Seek international recognition of the accreditation system, including applying for an EA-MLA signature status.
- Improve availability of domestic conformity assessment services and develop the country's market surveillance system.
- Align accreditation and conformity assessment legislation, increase EN standards adoption for EU *acquis* harmonization.
- Provide financial support and specific conditions for SMEs to access standards.
- Formulate SMEs' requirements in standardisation and develop measures to facilitate their access to conformity assessment.
- Implement digitalisation strategies for government, economy, and society, employing a digital toolkit for technical regulators.
- Introduce support programmes for cluster development and business linkages to facilitate integration into GVCs.
- Explore matchmaking and incentives for FDIs, including tax credits for foreign-invested firms supporting domestic suppliers.
- Create a robust monitoring system to improve accountability and effectiveness of programs aiding SMEs' global market access.

**Fostering innovation and business support**

- Identify a co-ordinating agency with a strong mandate for SME support and design, with a dedicated SME digitalisation programme.
- Leverage the existing ecosystem of external advisors to enhance support services for SMEs.
- Integrate ICT use by businesses as a regular statistical output of Armstat, building on the pilot survey.
- Improve policy coherence by consolidating innovation support measures into a comprehensive national strategy.
- Improve monitoring to gauge lasting financial support impact on business innovation.

- Develop a comprehensive strategy for SMEs to promote green practices, including training on environmental management systems.
- Identify a dedicated unit for SME support in greening efforts and introduce tax incentives and financing options.
- Implement monitoring and evaluation to assess the impact of incentives on SME greening and inform policy decisions.

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## Notes

[1] For more information on the analytical framework, please refer to the thematic chapter “Digital Economy for SMEs”.

[2] Armenia’s e-draft.am platform is the Unified website for publication of legal acts’ drafts. Powered by the Ministry of Justice and funded by the EU, this website enables online public consultations of draft bills by the public.

[3] e-gov.am/licenses

[4] See https://impactaim.com/en/accelerators/challenge/accelerator-5.

[5] The development of a comprehensive legal and regulatory framework for crowdfunding was supported by the EBRD.

[6] Additional planned measures include a pilot programme targeting businesses active in the sectors of textile, footwear and leather production. Selected businesses will be offered consultancy services regarding access to e-commerce platform such as Amazon and Walmart. The programmes also foresee partial reimbursements of the costs businesses face to access the platforms.

[7] The OECD Trade Facilitation Indicators were launched in 2013 and since then have been updated every two years. The 2020 SBA Assessment considered the 2017 update of the TFIs, as the 2019 update was not yet available at the time of drafting. The 2024 Assessment considers the 2022 update.

[8] https://www.eif.am and https://impactaim.com/en

[9] Data collected with this methodology for OECD countries that are part of the European Statistical system appear in the OECD database ICT Access and Use by Businesses

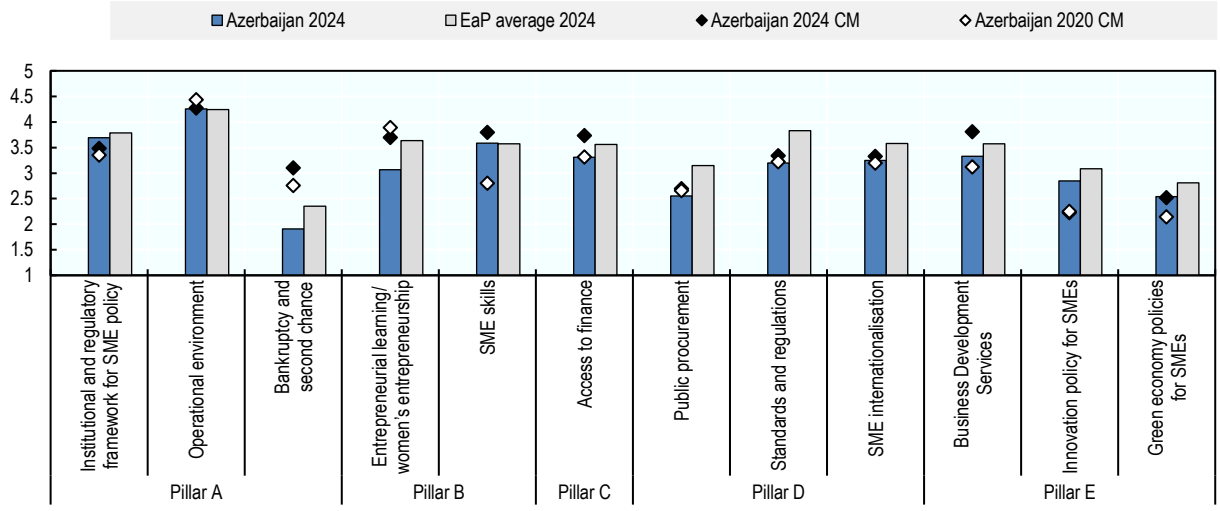
# 11 Azerbaijan: Small Business Act country profile

This chapter provides an assessment of the progress made by Azerbaijan in implementing the Small Business Act (SBA) for Europe over the period 2020-23. It starts with an overview of Azerbaijan's economic context and dives further into the characteristics of the country's SME sector. It then develops on the state of selected framework conditions for the digital transformation of SMEs. Finally, it analyses Azerbaijan's progress along twelve measurable dimensions grouped in five thematic pillars and sets out targeted policy recommendations.

## Key findings

### Figure 11.1. SME Policy Index scores for Azerbaijan

Country scores by dimension, 2024 and 2020 vs 2024 CM




Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### Table 11.1. SME Policy Index scores for Azerbaijan

Country scores by dimension, 2024 and 2020 vs 2024 CM

| Pillar | Dimension | Azerbaijan 2024 | EaP average 2024 | *Azerbaijan 2024 (CM)* | *Azerbaijan 2020 (CM)* |
|---|---|---|---|---|---|
| Pillar A | Institutional and regulatory framework for SME policy | 3.69 | 3.78 | 3.49 | 3.36 |
| | Operational environment | 4.25 | 4.24 | 4.28 | 4.44 |
| | Bankruptcy and second chance | 1.91 | 2.35 | 3.10 | 2.76 |
| Pillar B | Entrepreneurial learning/ women's entrepreneurship | 3.07 | 3.64 | 3.70 | 3.89 |
| | SME skills | 3.59 | 3.57 | 3.80 | 2.80 |
| Pillar C | Access to finance | 3.31 | 3.56 | 3.74 | 3.32 |
| Pillar D | Public procurement | 2.55 | 3.15 | 2.70 | 2.66 |
| | Standards and regulations | 3.20 | 3.83 | 3.34 | 3.23 |
| | SME internationalisation | 3.25 | 3.58 | 3.33 | 3.20 |
| Pillar E | Business development services | 3.33 | 3.57 | 3.81 | 3.12 |
| | Innovation policy for SMEs | 2.85 | 3.09 | 2.22 | 2.25 |
| | Green economy policies for SMEs | 2.54 | 2.81 | 2.52 | 2.15 |

Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Table 11.2. Implementation progress on SME Policy Index 2020 policy reforms – Azerbaijan

| Priority reforms outlined in the SME Policy Index 2020 | Key reforms implemented to date |
|---|---|
| **Pillar A – Responsive Government** | |
| Expand "Roadmap for the Promotion of the Production of Consumer Goods by SMEs in Azerbaijan" to include the services sector.<br>Ensure that the SME Development Agency (KOBIA) responds to the needs of small businesses.<br>Introduce measures to upgrade the IT skills of small entrepreneurs.<br>Establish effective channels of consultation with organisations representing the entire SME sector.<br>Define the regulatory impact assessment (RIA) guidelines and methodology and identify the leading body in charge of RIA applications.<br>Promote alternative dispute resolution and simplified proceedings for SMEs.<br>Adopt a proactive second-chance strategy for bankrupt entrepreneurs. | Inclusion of SME policy measures in the Socio-Economic Development Strategy of the Republic of Azerbaijan 2022-2026.<br>Establishment of the Public Council under KOBIA as the main channel of public-private consultations for SME policy.<br>Systematic review of business legislation by the Commission for Business Environment and International Ranking.<br>Establishment of an RIA division within the Ministry of Economy with reports made publicly available.<br>Amendment of the Insolvency Law in December 2020 to clarify the grounds for debtor insolvency and creditors' voting rights. |
| **Pillar B – Entrepreneurial Human Capital** | |
| Introduce the entrepreneurship key competence at system level across all levels of education.<br>Prioritise the independent evaluation of women's entrepreneurship support programmes and build-in engagement by non-government policy partners.<br>Focus on the availability and quality of data for policy making and ensuring effective provision of SME training services for different target groups. | Integration of an entrepreneurship module into the vocational education and training (VET) curricula; further development of infrastructure and career guidance services.<br>Progress in non-formal learning and awareness-raising.<br>Establishment of women's resource centres in regions; increase public-private co-operation on women's entrepreneurship.<br>Development of a framework for the collection and analysis of data of SME skills used to inform policymaking.<br>Development of a network of operators by KOBIA to improve training provisions. |
| **Pillar C – Access to Finance** | |
| Enhance financial inclusion by supporting the development of non-bank financial services and deepening credit information.<br>Adopt a new law on leasing.<br>Improve the availability of statistical data on the financial sector to enable a more granular market assessment and develop products tailored to the needs of borrowers. | Implementation of the Basel III principles.<br>Adoption of an enhanced risk-based supervision and stress-testing model.<br>Establishment of the first local venture fund "Caucasus Ventures".<br>Establishment of various portals and platforms to improve financial literacy. |
| **Pillar D – Access to Markets** | |
| Ensure a co-ordinated approach and build KOBIA's capacity to support SME internationalisation.<br>Enhance SME access to trade financing and implement a support programme to create supply chain linkages between SMEs and large investors.<br>Strengthen the national accreditation body and make it fit to enter into a bilateral agreement with EA.<br>Implement targeted SME training and standardisation.<br>Provide financial support for SMEs to implement technical standards.<br>Ensure the use of e-procurement in a wider range of award procedures.<br>Raise status, independence, capacity of central procurement institutions. | National Plan for 2023-2025 on harmonisation of standardisation with international requirements and adoption of EU standards.<br>Introduction of financial support for SMEs to acquire standards.<br>Promotion of the use of e-commerce as an objective of the 2022-2026 Socio-Economic Development Strategy.<br>Establishment of an online sales platform to support SMEs. |
| **Pillar E – Innovation and Business Support** | |
| Organise innovation policies under a single national strategy.<br>Establish co-ordination mechanisms among bodies providing business development services (BDS).<br>Extend eligibility of grants for innovation beyond the IT sector.<br>Build capacity of KOBIA and sub-structures' staff to advise businesses.<br>Outsource support services to private BDS providers and/or offer a co-financing mechanism to SMEs for first-time BDS use.<br>Target green-economy policies towards the capacities and needs of SMEs. | SME-related innovation policies included in the Socio-Economic Development Strategy 2022-2026.<br>Outreach to SMEs ensured by KOBIA's network of sub-structures (SME Houses, SME Development Centres and SME Friends).<br>Introduction of a "startup certificate" for micro and small businesses for the sale of innovative products or services.<br>Creation of KOBIA's grant competitions for entrepreneurs.<br>Regulatory and financial instruments to promote greening practices among SMEs, including via Entrepreneurship Development Fund. |

## Context

### *Economic snapshot*

As a major exporter of hydrocarbons, Azerbaijan benefitted from the sharp increase in oil and gas prices triggered by Russia's full-scale invasion of Ukraine. GDP growth reached 4.7% in 2022, further sustaining the post-COVID-19 recovery following a decline of 4.3% in 2020 (Table 11.3). Nevertheless, as a negative consequence of the pandemic and the war, inflation rose to 6.7% in 2021 and further accelerated to almost 14% in 2022, driven by high global commodity and food prices (IMF, 2023[1]).

Azerbaijan imports about 30% of its wheat from Russia and is consequently making efforts to diversify its food supplies (OECD, 2023[2]). Additionally, due to its currency peg to the US dollar, imported inflation through increasing food prices was avoided (Central Bank of the Republic of Azerbaijan, 2023[3]).

Azerbaijan's economy is dominated by mining and quarrying activities, mainly related to the extraction of crude petroleum and natural gas, accounting for 45% of GDP in 2022 (SSCRA, 2023[4]), while mineral fuels and oils account for the highest share of exported goods (88% in 2021) (SSCRA, 2023[5]). The country has the potential to cater to the EU's efforts to reduce its energy dependence on Russia, especially after the completion of the Southern Gas Corridor. Thus, the dominance of the energy sector is unlikely to change in the near future. That said, although the sector generates high revenues, the sector provided jobs for less than 1% of the population in 2022. In contrast, the agricultural sector accounted for more than a third of employment in 2022, while generating only 4.8% of value added (SSCRA, 2023[6]).

However, Azerbaijan has adopted policies to diversify its economy, notably through its 12 Strategic Roadmaps for 2016-2020 and the Socio-Economic Development Strategy for 2022-2026. The latter reform plan introduces a private-sector-led growth model and seeks to enhance human capital, with a target of sustained 5% growth in non-energy sector during the 2022-2026 period (World Bank, 2023[7]). For 2022 alone, non-energy sector growth was recorded at 9.1% (year-on-year) and driven by services, including ICT (World Bank, 2023[7]). While the ICT sector is seen as instrumental and a potential driver of economic diversification in Azerbaijan, the share of the information and communication sector in the value-added generated in Azerbaijan reached its lowest point in 2022 with 1.4% – against annual results ranging from 1.6% to 2.1% between 2012 and 2021. In addition, the sector's share in the average annual number of workers has stabilised at 1.9% or slightly below in recent decades (SSCRA, 2023[8]). Consequently, the share of the ICT sector in Azerbaijan's GDP has decreased to 1.4% in 2022 against 1.8% in 2016 (SSCRA, 2022[9]).

Despite the ICT sector's modest size, a significant share of Azerbaijani enterprises started or increased online business activity during COVID-19 – 60% of small enterprises, 71% of middle-sized firms, and 52% of large companies (World Bank, 2021[10]). Thus, SME growth has most to benefit from an expansion in the ICT sector. Nevertheless, SMEs are still lagging behind in adopting solutions, and the range of services offered for SMEs in non-ICT sectors to catch up remains limited (OECD, 2022[11]). Given the potential of the sector's services to support all SMEs' development and digitalisation, Azerbaijan has much to gain economically in boosting the productivity of its ICT sector.

### Table 11.3. Azerbaijan main macroeconomic indicators 2018-2022

| Indicator | Unit of measurement | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|
| GDP growth** | Percentage, year-on-year | 1.5 | 2.5 | -4.2 | 5.6 | 4.7 |
| Inflation** | Annual percent increase, consumer prices | 2.3 | 2.7 | 2.8 | 6.7 | 13.9 |
| Government balance** | Percentage of GDP | 5.4 | 8.9 | -6.6 | 4.1 | 6.1 |
| Current account balance** | Percentage of GDP | 12.8 | 9.1 | -0.5 | 15.2 | 30.5 |
| Exports of goods and services* | Percentage of GDP | 54.1 | 49.1 | 35.6 | 46.5 | 60.1 |
| Imports of goods and services* | Percentage of GDP | 37.6 | 36.8 | 36.4 | 29.8 | 27.0 |

| Indicator | Unit of measurement | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|
| FDI net inflows* | Percentage of GDP | 3.0 | 3.1 | 1.2 | -3.1 | -5.7 |
| General government gross debt** | Percentage of GDP | 18.7 | 17.7 | 21.3 | 26.5 | 20.7 |
| Domestic credit to private sector* | Percentage of GDP | 20.8 | 23.0 | 26.0 | 22.9 | 18.3 |
| Unemployment* | Percentage of total active population | 4.9 | 4.9 | 7.2 | 5.9 | 5.5 |
| Nominal GDP** | USD billion | 47.1 | 48.2 | 42.7 | 54.6 | 69.9 |

Note: Government balance corresponds to General government net lending/borrowing; unemployment reflects modelled ILO estimates
Sources: * (World Bank, 2023[12]); ** (IMF, 2023[1]); both accessed May 2023, ***OECD Calculations based on (World Bank, 2023[12]) and (SSCRA, 2023[5])

### Box 11.1. Azerbaijan's support for SMEs during the COVID-19 pandemic

**Financial support**

During the COVID-19 pandemic, the Azerbaijani government offered support for businesses and individuals totalling 4.85% of the country's GDP. This included additional funds for the Entrepreneurship Development Fund as well as AZN 80 million (EUR ~44.5 million) dedicated to microentrepreneurs.

In sectors negatively affected by the pandemic, businesses were offered the possibility to apply for state guarantees for 60% of the loan amount and a 50% interest rate subsidy on selected new loans, as well as an 10% interest rate subsidy on existing loans for a year. Unsecured microloans were distributed to the agricultural sector.

**Regulatory flexibility**

In 2020, deadlines for tax declarations and payment were extended. Azerbaijan amended its Tax Code and introduced temporary tax benefits and holidays to minimise negative effects on businesses. Measures included reductions in profit tax and social security contributions for businesses that were particularly impacted by the pandemic. Workforce support

The government provided AZN 215 million (EUR ~120 million) to partially cover the salaries of 300,000 employees. Unemployed and low-income citizens that lost earnings due to the pandemic also received a lump-sum payment of AZN 190 (EUR ~106). Taxpayers in sectors particularly affected by the pandemic were exempted from 75% of their income tax, from land and property tax for one year, and from rental tax for nine months.

The government also sought to provide assistance for individual entrepreneurs, as well as for business owners, to help pay wages through an online platform by transferring funds directly to their bank accounts. By the end of July 2020, almost 30,000 entrepreneurs had used it to pay salaries worth a total of almost AZN 98 million (EUR ~54.5 million).

Source: (IMF, 2021[13]), (OECD, 2020[14]).

## *SME sector*

A new definition of SMEs was introduced in December 2018 with the objective of eliminating differences in the methodologies applied by the State Statistical Committee and the Ministry of Taxes. The new definition distinguishes between micro, small, medium-sizes, and large enterprises, and is aligned with the EU definition regarding the thresholds used for number of employees.

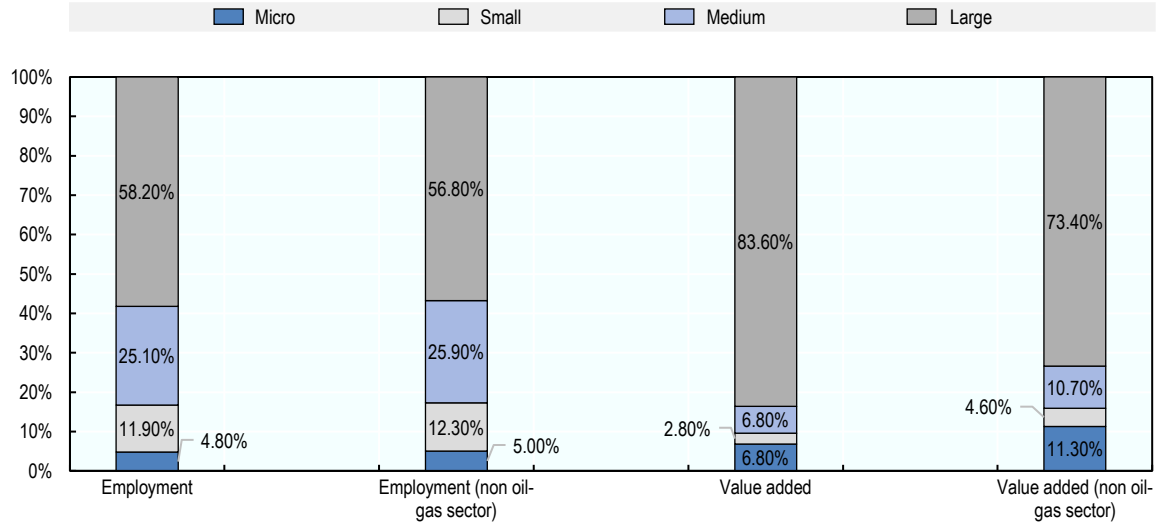
## Table 11.4. Definitions of SMEs in Azerbaijan

| | Micro | Small | Medium |
|---|---|---|---|
| Number of employees | < 10 employees | < 50 employees | < 250 employees |
| Turnover | < AZN 200 000 (EUR ~111 650) | < AZN 3 000 000 (EUR ~1 674 747) | < AZN 30 000 000 (EUR ~16 747 470) |

Note: Exchange rates as of 28 September 2023 (OANDA, n.d.[15]).
Source: Resolution No. 556 of the Cabinet of Ministers of the Republic of Azerbaijan dated 21 December 2018.

The economic potential of SMEs in Azerbaijan remains largely untapped. SMEs generated 16.4% of value added and accounted for 41.8% of total employment in 2021 (Figure 11.2). In the non-oil sector, SMEs generated 26.6% of value added and accounted for 43.2% of employment in 2021. While the value added of the non-oil sector has increased slowly but steadily in recent years (mostly driven by small enterprises), the share of employees in non-oil SMEs has shrunk by about 2 percentage points, to 43% in comparison to 45% in 2018 (SSCRA, 2022[16]; OECD et al., 2020[17]).

## Figure 11.2. Business demography indicators in Azerbaijan, by company size (2021)



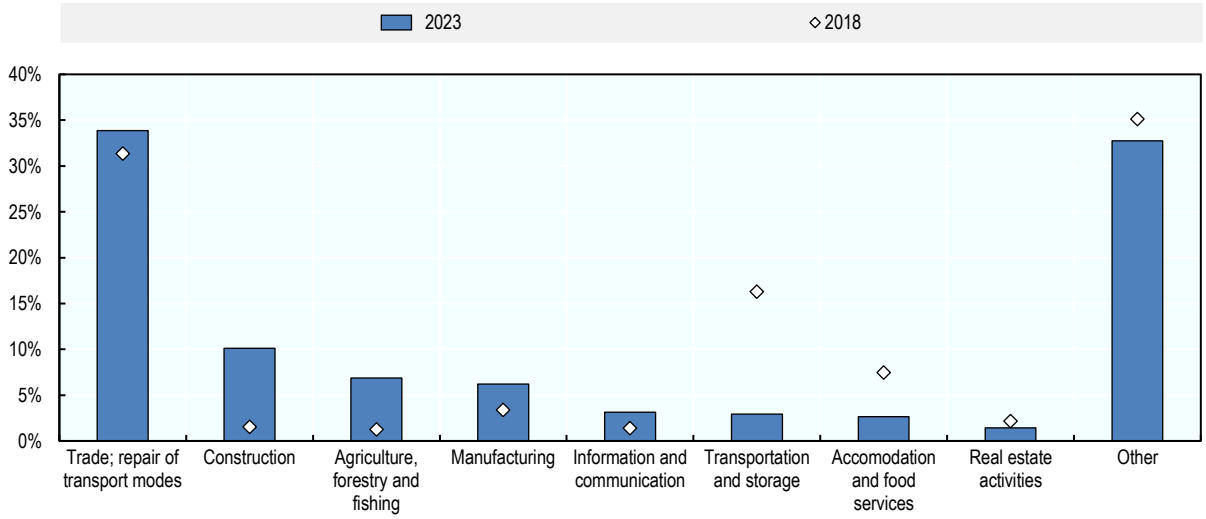

Source: Azerbaijan State Statistical Committee (SSCRA, 2022[16]).

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Most Azerbaijani SMEs are concentrated in relatively low value-added activities, such as trade and repair of vehicles, construction, and agriculture (Figure 11.3). The number of SMEs operating in these sectors changed substantially between 2018 and March 2023. The importance of the construction sector increased to a share of 10% of SME activity from 2% in 2018. Also, the agricultural sector has become more relevant for SMEs, with an increase to a share of 7% of SMEs. By contrast, the transport sector experienced a substantial decline of SMEs accounting for a share of only 3%.

### Figure 11.3. Sectoral distribution of SMEs in Azerbaijan as of March 2023

Share of SMEs by type of economic activity




Note: "Other" includes mining and quarrying, electricity, gas and steam production and supply, water supply, waste management, financial and insurance activities, professional, scientific, and technical activities, administrative and support service activities, education, human health and social work, arts/entertainment/recreation, and other service activities.
Source: OECD calculation based on data from Azerbaijan State Statistical Committee.

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## SBA assessment by pillar

### *SME digitalisation policies*

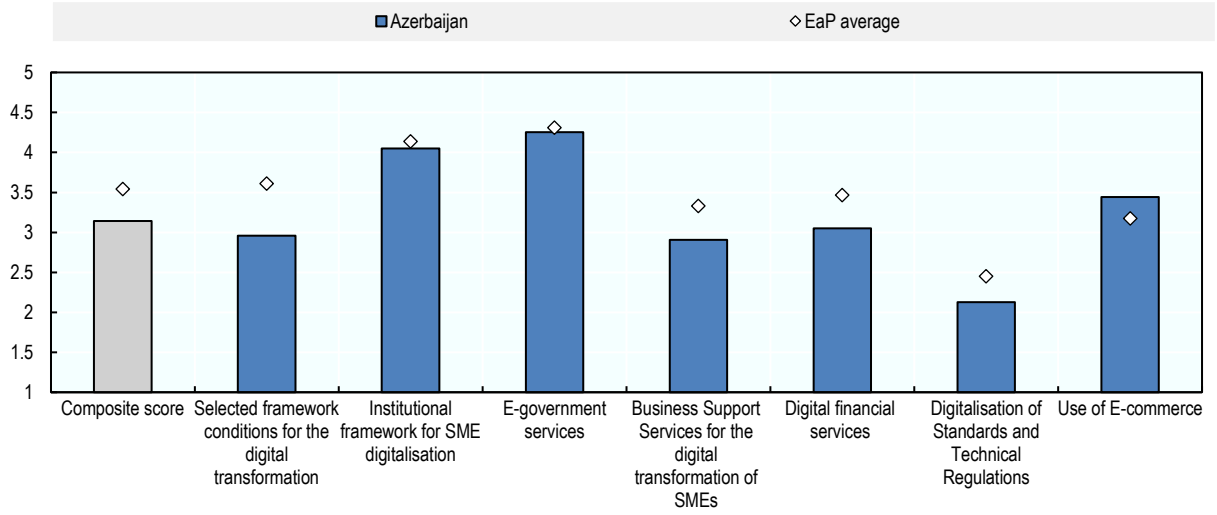
Creating an environment conducive to the digital transformation of SMEs requires a comprehensive policy approach based on sound framework conditions for the digital economy as well as targeted support to help SMEs reap the benefits of digital solutions. Framework conditions refer to pre-requisites for the digital transformation, such as affordable access to high-speed broadband, a satisfactory level of digital literacy among citizens, and a well-co-ordinated and coherent policy approach and governance system for digital policies. In the context of SME development, those fundamentals need to be complemented with specific business support services, digital financial services for SMEs, and tailored support to engage in e-commerce to reach new markets.

Reflecting the multi-faceted nature of the topic, this round of SBA assessment evaluates EaP countries' policy approaches to SME digitalisation through i) a dedicated pillar on selected framework conditions for the digital transformation, as well as ii) six new sub-dimensions, incorporated in the pre-existing dimensions of the SBA assessment, to delve deeper into specific thematic policies to foster the digital transformation of SMEs. The weighted average of the scores for the new pillar and digitalisation-oriented sub-dimensions results in a composite score for SME digitalisation policies presented below (Figure 11.4).[1]

Azerbaijan's composite score of 3.14 for SME digitalisation policies is driven by its institutional framework in that regard, with the *Socio-Economic Development Strategy of the Republic of Azerbaijan 2022-2026* (SEDS) addressing the issue and the co-ordination efforts between stakeholders, as well as the sharp improvements in the provision of e-government services. The country also ranks among the top regional performers in terms of e-commerce, thanks to the measures planned in the SEDS, dedicated support for

SMEs and the existence of a regulatory framework. On the other hand, Azerbaijan should pursue its efforts to create robust framework conditions (notably by adopting a national digital strategy (NDS), enhancing the collection of internationally comparable data and improving high-speed Internet accessibility), step up business support services for the digital transformation, and work on the digitalisation of standards and technical regulations.

## Figure 11.4. Scores for SME digitalisation policies in Azerbaijan




Note: Further details on the assessment and calculation methodology can be found in the "Assessment framework" section in the "Digital Economy for SMEs" chapter, in the "Policy framework, structure of the report and assessment process" chapter and in Annex A. Additional information on institutional framework for SME digitalisation and e-government services can be found in Pillar A; on digital financial services in Pillar C; on use of e-commerce in Pillar D; and on business support services for the digital transformation of SMEs in Pillar E.

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The following section details Azerbaijan's performance in developing selected framework conditions for the digital transformation, while more information on digitalisation-oriented sub-dimensions can be found in the sections on the pillars they respectively belong to.

### *Selected framework conditions for the digital transformation*

Individuals and firms, notably SMEs, cannot fully reap the benefits offered by the digital transformation without the existence of robust framework conditions, such as comprehensive digitalisation policies, access to high-speed Internet and well-rounded ICT skills among the population. Accessible, affordable and stable broadband connection is indeed the *sine qua non* to ensure widespread participation of citizens and businesses in the digital economy, and to stem the widening of the connectivity gaps between urban and rural territories, and between firms of different sizes. Furthermore, fostering digital skills development at all stages of life (through formal education and lifelong learning initiatives for adults) is essential to help the working-age population acquire the skills they need to embark on the digital transformation, produce tech-savvy consumers, and build a talent pool of IT specialists.

#### *National digital strategy*

Azerbaijan has been making policy efforts to accelerate the digital transformation of its economy and society. The *Strategic Roadmap for Development of Telecommunications and Information Technologies* (ICT Roadmap) and the *Strategic Roadmap for the Production of Consumer Goods at the Level of Small*

*and Medium Enterprises in the Republic of Azerbaijan* (SME Roadmap), adopted in 2015, fostered the implementation of several measures for digitalisation between 2016 and 2020, such as the development of the digitalisation of public services and financial tools to help SMEs acquire digital technologies. More recently, in January 2023, Azerbaijan adopted a so-called "ICT package" notably entailing legislative changes to further encourage the growth of the IT sector. Regarding the digital transformation of the economy at large, measures are currently foreseen in the *Socio-Economic Development Strategy of the Republic of Azerbaijan 2022-26 (SEDS)*, which foresees, in its Action Plan approved in July 2022, the creation of a standalone National Digital Strategy, the *Digital Economy Strategy*. The latter should be finalised by the end of 2023.

For the preparation of this upcoming document, Azerbaijan has worked towards co-ordinating efforts across stakeholders. The design of the new strategy was assigned to the Ministry of Economy and, within the Ministry, the Centre for Coordination and Analysis of the Fourth Industrial Revolution (Box 11.2). A dedicated Working Group on the Preparation of the Digital Economy Strategy was established by Order of the Minister of Economy of the Republic of Azerbaijan dated 12 December 2022, aiming at ensuring internal co-ordination and co-operation with international donors and consulting organisations. The institutions involved include the Central Bank, the Ministry of Digital Development and Transport, the Ministry of Science and Education, the Ministry of Finance, the State Service for Special Communication and Information Security, the State Agency for Public Service and Social Innovations under the President of the Republic of Azerbaijan, relevant structures of the Ministry of Economy, and external consultants.

While the SEDS sets targets to assess the implementation of the planned measures, Azerbaijan collects only a limited number of indicators related to the digital transformation of SMEs specifically – which might hinder impact evaluation.

Moving forward, Azerbaijan should ensure the adoption of a comprehensive policy approach in its upcoming National Digital Strategy. It should also include provisions for the digital transformation of non-IT sectors, notably SMEs – as this aspect would benefit from additional efforts. To ensure concrete impact, the strategy will need to set clear objectives, associated with sufficient budget/resources and targets, and process- and result-oriented key performance indicators to allow for the monitoring and evaluation of each policy action. Since limited co-ordination during the implementation of previous policy documents has been lowering the impact of policy initiatives (OECD, 2022[11]), Azerbaijan should pursue a multi-stakeholder approach, building on the newly established working group, and also involve private sector representatives to ensure all views are taken into account. Finally, Azerbaijan could consider collecting additional data, in line with EU and OECD methodologies, to enable better assessment of policy measures and international comparisons.

### *Broadband connectivity*

Azerbaijan has made significant policy efforts to develop broadband connectivity in recent years. Several policy documents have been adopted and implemented, such as the *Telecom Road Map 2017-2020* and the Regional Development Plans for 2009-13, 2014-18, and 2019-23. The above-mentioned ICT Roadmap also sets targets towards improving access to broadband across the Azerbaijani territory. A strategy and action plan on broadband for 2021-24 have reportedly been adopted, although the documents are not available online.

In terms of recent achievements, Azerbaijan has made considerable improvements in fixed broadband speed in recent years, notably fostered by government investment in infrastructure, but uptake levels remain below those of its EaP and OECD peers. The government has planned further measures to improve the situation, including the development of a new regional fibre-optic network, the Trans-Eurasian Information Superhighway, and the broadband strategy reportedly aims at having 100% of households covered and a minimum download speed of 25 Mbps by 2025. Despite being below EaP averages for fixed and mobile broadband uptake, Azerbaijan has made progress in reducing digital divides between urban

and rural areas, with the current gap appearing quite low according to International Telecommunication Union (ITU) data (see Figure 4.4. in the "Digital Economy for SMEs" chapter). Azerbaijan also has one of the highest shares of individuals using Internet across the EaP region.

However, broadband subscriptions are still below OECD and EU levels, and Internet affordability has slightly decreased in recent years. Azerbaijan collects a range of data on digital divides, which offer up-to-date insights on broadband uptake by different target groups. This notably reveals persisting challenges in terms of businesses' Internet access, with barely half of Azerbaijani firms having an Internet connection.

Moving forward, Azerbaijan should pursue its efforts to foster access to high-speed Internet across its territory. To this end, it could consider i) lowering barriers to broadband access through regulation and policies designed to enable investment, while safeguarding competition and investment incentives; ii) implementing measures to strengthen the resilience of communication networks, such as network diversity and redundancy, to reduce connection disruptions; iii) increasing digital literacy, as the lack thereof remains a challenge to broadband uptake in rural areas; and iv) conducting regular multi-stakeholder meetings, including with network providers, consumers and local authorities.

### *Digital skills*

Digital skills policies are included in the SEDS 2022-26. The latter foresees the implementation of digital literacy at all education levels, the creation of educational resources, and lifelong learning initiatives. The topic was previously mentioned in the ICT Roadmap and also embedded in national legislation – such as the national qualifications framework (NQF) approved by the Cabinet of Ministers in 2018 (outlining digital skills at all levels of education) and the general education legislation that includes digital competence as a key competence for vocational education and training (VET) and lifelong learning.

With regard to education systems, the SEDS foresees the introduction of awareness-raising campaigns and the development of an "ICT-based infrastructure" in education facilities, as well as training for teachers and managers and the improvement of ICT materials, notably computers. It also provides for the creation of educational resources for educators, students, and parents, and an increase of graduates in tech fields. As for lifelong learning opportunities, Azerbaijan seeks to improve the quality and accessibility of digital skills training. To this end, a "digital academy" will be created, providing training and re-training for management professionals, starting with civil servants.

In addition to these policy plans, several initiatives have already successfully been implemented – such as courses in science, technology, engineering, and mathematics (STEM) offered to children and students by the Innovation and Digital Development Agency (IDDA); the Digital Skills project of the Ministry of Education; and additional courses provided to individuals and businesses by the Information-Communication Technologies Application and Training Centre under the Ministry of Digital Development and Transport. One of the latest milestones in the country lies in the development of the IT Hubs project, implemented jointly by the C4IR, EBRD and StrategEast company. It will offer 11 months of training in such areas as computer science, programming and business analysis to people between the ages of 19 and 30 in different regions and cities of Azerbaijan, with the aim of increasing their employability. Further training opportunities are being developed by the C4IR, as mentioned in Box 11.2.

### Box 11.2. Azerbaijan's Centre for Analysis and Coordination of the Fourth Industrial Revolution (C4IR)

Established in 2021 by and within the Ministry of Economy of the Republic of Azerbaijan, the Centre for Analysis and Coordination of the Fourth Industrial Revolution (C4IR) focuses primarily on analysing and co-ordinating challenges, initiatives, strategies and projects related to the digital economy.

Working in collaboration with public- and private-sector partners, as well as academia, the Centre aims to develop and test policies and regulatory frameworks designed to harness the potential of key emerging technologies with the goal of positioning the country as a leader in the field.

The "Fourth Industrial Revolution" (4IR) – characterised by the convergence of digital, biological and physical technologies – is profoundly transforming economies, industries and societies. C4IR endeavours to capitalise on these changes to drive opportunities and benefits for Azerbaijan's development in the digital era.

The Centre's activities include:

- **Policy analysis**: The Centre conducts analyses of emerging technologies' impact on various sectors, identifying potential policy implications. It offers research-based recommendations to policy makers, fostering an enabling environment that promotes innovation while safeguarding privacy, security and ethics.
- **Collaboration and co-ordination**: Serving as a platform for collaboration, C4IR facilitates partnerships among diverse stakeholders, including government agencies, private sector companies, academic institutions and civil society organisations. The goal is to encourage innovation and shared approaches to 4IR related issues.
- **Pilot projects and prototyping**: The Centre often undertakes pilot projects and prototyping initiatives to demonstrate the practical applications of emerging technologies. These projects showcase how new technologies can be integrated into industries and society, leading to positive outcomes.
- **Capacity building**: C4IR plays a crucial role in enhancing digital skills and capabilities among individuals and organisations to adapt to the demands of the 4IR. This includes offering training programmes, workshops and awareness campaigns designed to empower stakeholders to harness the potential of new technologies effectively.

For example, the Centre collaborates with the US company Coursera and both parties signed an agreement to provide a wide range of courses covering programming, artificial intelligence, big data, machine learning, blockchain and cloud technologies. The project will also provide access to courses on leadership, communication and English language skills. Offered in collaboration with relevant government agencies, these courses will contribute to advancing digital literacy and skills development in Azerbaijan.

Source: (World Economic Forum, 2023[18]).

Nevertheless, digital skills levels in Azerbaijan remain below those of the country's EaP, EU and OECD peers, with almost half of the population having only basic digital skills. No dedicated educational framework yet exists for fostering digital skills from initial schooling onwards, and data reveal considerable urban-rural gaps in schools across the country, e.g. in terms of pupils using the Internet. While Azerbaijan has some data on levels of basic and standard digital skills, insights remain scarce, with a lack of information on, for example, the levels of advanced digital skills in the population and of digital literacy among firms' managers and employees. Azerbaijan also does not yet have digital skills anticipation tools

in place – these are only conducted on an ad hoc basis, by international donors. The country is, however, implementing a pilot project jointly led by the Statistical Office, the Ministry of Digital Development and Transport and ITU this year, to assess digital skills among households, university students, and public and private sector employees, but results are not yet available.

Moving forward, Azerbaijan should i) strengthen skills assessment and anticipation tools, and notably adopt a digital competence framework to provide a benchmark against which to measure skills levels among individuals and businesses (in line with the EU's Digital Competence Framework, or DigComp) to ensure international comparability and recognition; ii) ensure digital skills training opportunities across the country, to bridge current divides; and iii) foster the development of a multi-stakeholder approach on digital skills policies, ensuring the involvement and co-ordination of all relevant actors, including education providers, local authorities and firms.

## *Pillar A: Responsive Government*

### *Institutional and regulatory framework*

Since 2020, Azerbaijan has consolidated the achievements made on the institutional and regulatory framework for SME policy under the 2016-2020 SME Road Map, expanded the SME support network, and made further progress in upgrading the legislative framework concerning SMEs.

The government's main policy priority remains the improvement of the operational environment for SMEs and the diversification of the country's economic structure. Therefore, SME policy is seen as an integral component of the country's socio-economic strategy.

#### Institutional setting

The SME policy mandate in Azerbaijan is placed under the Ministry of Economy and specifically under the Department for Entrepreneurship Development. SME policy is conducted and implemented by the Small and Medium Business Development Agency (KOBIA) operating under the Ministry of Economy. Other agencies and public bodies relevant for SME policy are the Commission for Business Environment and International Ranking under the Presidential Administration, which is in charge of promoting and co-ordinating regulatory reforms; the Centre for the Analysis of Economic Reforms and Communications (CAERC), which handles reform planning and monitors the implementation of the reform plans; and the Innovation and Digital Development Agency, placed under the Ministry of Digital Development and Transport, whose mandate involves promoting the development of an ecosystem supporting innovation, the development of e-government services, and enterprise digital transformation.

The implementation of the SME Road Map was completed in 2020 and it has reached most of its objectives, particularly with regard to the establishment of KOBIA and the network of SME support bodies. CAERC has monitored the Road Map implementation and conducted a review of SME Road Map achievements.

At present Azerbaijan does not have a specific multi-year SME strategy. Its main SME policy directions and measures are presented in the SEDS 2022-26 under National Priority One: sustainable and growing competitive economy – promotion and sustainable and high economic growth. The government opted to include SME policy objectives in the broader national development strategy in order to ensure cohesion and co-ordination of SME policy measures with the country's broader economic development and productive diversification strategy. Activities related to SMEs are distributed among different thematic chapters of the Socio-Economic Development Strategy. The implementation of the Socio-Economic Development Strategy is conducted by CAERC, which regularly reports to the Presidential Administration and the Council of Ministers.

As planned in the Strategy, the government has recently approved three legislative acts concerning SMEs. The first act facilitates the distribution of SME products by large commercial companies, while the second act promotes cluster development (see below). Finally, the Law "On the Development of Micro, Small and Medium Enterprises", adopted at the end of 2022, defines the forms and methods for providing state support to micro, small and medium enterprises (MSMEs). The law covers various issues, including the goals, principles, and main directions of state policy for the development of MSMEs; conditions for providing support to entrepreneurial subjects; forms of support; procedures for monitoring and evaluation; and other areas including state financial support, advice and information support, and product production. In addition, the law provides for the establishment of a permanent group to co-ordinate activities in the field of development of MSMEs. Finally, the law foresees the creation of a single register of MSMEs.

As mentioned earlier, the main SME policy implementation body is KOBIA. The agency, established in 2017, has a total staff of 240 people and is at the centre of a network providing orientation and assistance to individual entrepreneurs, start-ups and small enterprises. The network consists of i) SME Development Centers, operating as structural divisions of KOBIA where professional trainers-experts provide business-oriented training, advice and support for business plan development and other services; and ii) SME Houses located in Baku, Khachmaz, and Yevlakh that operate as one-stop shops and provide services to entrepreneurs for all type of business activities, including business registration, tax issues, licenses, permits and certificates. The network also includes 45 SME Friends operating as KOBIA's local representatives. KOBIA conducts policy actions on the basis of a five-year action plan, complemented by six-month plans monitored by CAERC.

### Legislative simplification and RIA

The systematic review of business legislation, co-ordinated by the Commission for Business Environment and International Ranking under the Presidential Administration, has substantially contributed to an overall improvement of the business environment. According to the Ministry of Economy, over 50% of business-related legislation had been reviewed by the end of 2022. However, where new legislative acts and regulations are concerned, the adoption of regulatory impact assessment (RIA) is still at an initial phase and its application is relatively limited. The Law "On Licenses and Permits" dated March 15, 2016, mentioned RIA as one of the tools available for the evaluation of the impact of new state regulation in the field of licenses and permits. Elements of RIA are applied during the elaboration of new legislative acts and regulations resulting from the work conducted by the different committees operating under the Commission for Business Environment and International Ranking. An RIA division has been established within the Ministry of Economy, while the application of RIA methodology is supervised by the Legal Division of the Presidential Administration. All RIA reports are publicly available, and examples of RIA exist in other normative legal acts of the Republic of Azerbaijan. A recent example concerned the Law "On Environmental Protection" and specifically on legal and economic regulation related to environmental protection. However, RIA is currently applied to less than 25% of new law laws and regulations.

Azerbaijan has not formally applied an SME test to RIAs. However, according to Article 9.5 of Presidential Decree No. 148 dated June 26, 2018, all central and local executive authorities and municipal bodies, public legal entities created on behalf of the state, and legal entities whose shares are controlled by the state should make an assessment of how new legislative and normative acts affect the activity of MSMEs and should consult with KOBIA as part of the legislative and normative process.

The "Impact Assessment" section of the "Global Indicators of Regulatory Governance" (GIRG) Project implemented by the Global Indicators Group of the World Bank also reviewed and audited RIA applications in Azerbaijan and noted the absence of a single specialised state body for developing RIA's guidelines and conducting RIA.

#### Public-private consultations

Since 2020 Azerbaijan has made progress in promoting public-private dialogue. The Public Council operating under KOBIA functions as the main channel of public-private consultations in the SME policy area. In 2022, seven public discussions were organised under the umbrella of the Public Council. These events covered the topics of construction business, business opportunities in the creative industry, mediating disputes related to entrepreneurial activity, digital entrepreneurship, the role of private business in education, medical business, and agribusiness. More than 550 entrepreneurs participated in public discussions. KOBIA also manages the official website of the Public-Private Partnership (PPP) Development Centre (www.pppdc.gov.az), whose purpose is to inform interested parties within the framework of partnership relations between the public and private sectors, and to stimulate the implementation of PPP projects. Finally, it is important to mention the private sector participation in the committees operating under the Commission for Business Environment and International Ranking, which include representatives of state entities as well as private sector associations and other stakeholders.

#### Institutional framework for SME digitalisation

Promoting SME digitalisation is one of the objectives of the SEDS 2022-26. The topic of SME digitalisation is not covered by a specific section of the Strategy; instead, it is dealt with in the sections dedicated to the development of the digital economy, promoting digital skills and an innovation society. The Ministry of Economy and the SME Development Agency (KOBIA) are also members of the working group in charge of formulating the country's digital economy strategy and the implementation action plans, securing the co-ordination between the SME digitalisation objectives contained in the Socio-Economic Development Strategy and the country's strategy on the development of digital economy.

#### The way forward

Moving forward, Azerbaijan should ensure that all SME-related measures listed in the Socio-Economic Development Strategy are implemented in a timely fashion, that SME policies are backed by short-term action plans, and that the implementation of those actions is regularly monitored. For this purpose, the Ministry of Economy in association with KOBIA should publish a yearly report on SME development and economic structure diversification. Azerbaijan should also conduct regular public-private consultations (i.e. every three to six months) involving the Ministry of Economy, KOBIA, and representatives of the SME community (entrepreneurs, experts, local administration and NGOs) to review the implementation of SME objectives set in the Socio-Economic Development Strategy and to discuss measures related the country's contingent economic conditions. Finally, the country should upgrade the RIA methodology and bring it in line with international best practices and extend RIA to all new relevant primary and secondary legislative acts.

### *Operational environment for SMEs*

In the previous assessment, Azerbaijan scored above the EaP average in most of the sub-dimensions related to the SME operational environment, with the exception of business licenses. The improvement of the operational environment is one of the two main pillars of the country's SME policy, together with productive transformation. Since 2020, Azerbaijan has made incremental progress in improving the operational environment for SMEs, specifically in relation to the provision of e-services, driven by the COVID-19 pandemic.

Azerbaijan has taken a unique approach in the area of operational environment reform, bringing it under the supervision of the highest authority in the country. The Commission for Business Environment and International Ranking, operating within the Presidential Administration, acts as the main co-ordination body for regulatory reforms in this area. The Commission, chaired by the First Deputy Prime Minister, co-

ordinates the work of a number of committees, composed by government entities and representatives of private sectors and other stakeholders, covering several topics. Each committee targets a specific indicator related to the operational environment used by international institutions and aims at improving the country's performance and international ranking. Six of those committees are chaired by the Ministry of Economy, which is also a member of all other committees. The committees' work is monitored by CAERC, which ensures that their work is in line with the objectives set in the country's Socio-Economic Development Strategy.

#### E-government services

Over the last few years, Azerbaijan has made significant progress in the provision of the e-government services, in terms of both range and accessibility. The Azerbaijani Service and Assessment Network (ASAN) system, created in 2012 by the State Agency for Public Service and Social Innovations under the President of the Republic of Azerbaijan, provides access to a range of e-government services and is widely used by the population as well as by the business community, with terminals located in public spaces and in the ASAN service centres. The development of e-government is part of the Digital Azerbaijan project conducted by the E-Government Development Centre, a public entity operating under the State Agency for Public Services and Social Innovations. The objective of the project is to bring all e-government services under a single centrally managed portal. The IDDA is in charge of providing technical expertise to the various public administrations to lead to the establishment of the single portal for e-government services. It is also responsible for ensuring secure inter-operability across different public sector data banks and organising training courses in digital skills open to all categories of workers, in addition to promoting cyber security through a dedicated Cyber-security Centre.

#### Company registration

There have been no major changes in the company registration process since the last assessment. As before, the process is free of charge and can be conducted online through a dedicated website.

#### Business licensing

In the past, obtaining business licenses in Azerbaijan was a relatively complex process. However, since 2015 the government has acted to reduce the number of the licenses required. According to current legislation, the Ministry of Economy is in charge of issuing licenses for 23 types of entrepreneurial activity (excluding licenses issued by other authorities covering financial sector activities or activities concerning state security). Since 2020, the government has also reduced the average amount of the license fees by 50% and a further 50% discount is applied if the enterprise requires an additional license to operate in a province different from that of its headquarters.

In addition, license applications can now be made online through a "Licenses and Permits" portal (lisenziya.gov.az) managed by the Ministry of Economy. Launched in 2018, the portal was created to allow for the electronic issuance of licenses and permits and for the further improvement of the provided services, including the receipt of opinions from eight relevant institutions as part of the application process.

#### Tax compliance procedures for SMEs

Since 2019, the Tax Administration has introduced a number of measures to lower the tax burden on small enterprises and simplify tax administration procedures. Incomes of individuals who carry out entrepreneurial activities without creating a legal entity are subject to income tax at a rate of 20%, taking into account the expenses deducted from the income as determined by the Tax Code. A further simplified income tax regime is in place for individual entrepreneurs who have no employees. Income from dividends from entrepreneurial activities are exempted from taxes for shareholders/owners of enterprises not subject to VAT and a 75% tax reduction is in place for individual entrepreneurs.

The corporate income tax is set at 20%. However, enterprises that have obtained the “start-up” status from KOBIA benefit from a total corporate income tax exemption for a period of three years. In addition, the new Law on Clusters Development foresees income tax exemption for enterprises classified as member of clusters for a seven-year period, pending detailed regulations from the Ministry of Economy and the Tax Administration.

The evaluation of the efficiency of tax and customs incentives in effect or proposed in Azerbaijan is governed by the "Rules for the evaluation of the efficiency of tax and customs incentives" adopted by the Cabinet of Ministers of the Republic of Azerbaijan (Decision No. 436, dated 3 November 2020). The Ministry of Finance is the institution responsible for the Centralised Electronic Registry System of tax and customs incentives and exemptions.

#### The way forward

To continue improving the operational environment for SMEs, Azerbaijan should complete the elaboration of the country’s Digital Economic Strategy, making sure that it covers also the provision of e-government services and it is consistent with the Digital Azerbaijan Project.[2] The level of co-ordination among different institutions should be improved in order to develop a unique platform for accessing e-government services. Inter-operability among public sector data bases should also be improved. In addition, Azerbaijan should systematically monitor the usage of e-government services by different types of SMEs and promote digital skills among those enterprises that do not make use of those services. Finally, the country should develop effective monitoring mechanisms to assess whether the new tax incentives introduced with the legislative acts on start-ups and cluster enterprises have produced the expected results.

### *Bankruptcy and second chance*

Azerbaijan has taken some steps to improve its bankruptcy framework since the last SBA assessment. The Law No. 326-IQ “On Insolvency and Bankruptcy” (the Insolvency Law), adopted in June 1997 and last amended on in December 2020, remains the main legislative document regulating insolvency and bankruptcy procedures. The recent amendments clarify the grounds for insolvency of debtors willing to begin bankruptcy proceedings, regulate court hearings,[3] and clarify which creditors have a voting right on the recovery. Moreover, the Commission on Business Environment and International Ratings of the Republic of Azerbaijan has taken steps to further strengthen the current legislative framework by establishing a dedicated working group.

Although there are no particular incentives for extrajudicial voluntary agreements, the Insolvency Law allows the debtor to initiate insolvency proceedings with minimum involvement of the court. In this case, a creditors’ meeting is convened, and an insolvency practitioner is appointed by the court. However, this out-of-court procedure is led mainly by the creditors and the court is still involved in any approval of a reorganisation agreement concluded out of court. In addition, the insolvency framework does not foresee abbreviated or simplified procedures for small cases or SMEs. Statistics on insolvency proceedings are very limited and bankruptcy cases remain rare (in 2019 there were 18 bankruptcy cases before the administrative-economic courts, 16 of which were in Baku) (EBRD, 2021[19]). There is no monitoring mechanism in place to regularly assess the insolvency framework.

Measures to prevent insolvency remain insufficient. Although training in financial management is available to all businesses through KOBIA’s website, it is not specifically targeted at entrepreneurs in financial distress or fearing failure. Also, no early warning systems exist to help businesses identify potentially threatening financial conditions. Finally, although there are no restrictions imposed during the period of bankruptcy that might prevent entrepreneurs from a fresh start, there is no established and structured policy framework to promote second chance for honest entrepreneurs that go bankrupt.

## *Pillar B: Entrepreneurial human capital*

### *Entrepreneurial Learning*

Since the last SBA assessment, Azerbaijan has taken additional measures to promote entrepreneurial learning across education levels and the national population at large. Most progress has been achieved with regard to vocational education, with the entrepreneurship module being integrated into the VET curricula, in line with the State Standards of Vocational education adopted in March 2019. This allows students to acquire knowledge and skills in the field of entrepreneurial activity, organisation and planning of activities, such as business plan development. Azerbaijan has continued to develop VET infrastructure, such as the Sumgayit Vocational Education Centre inaugurated in 2020. Students also benefit from career guidance services through nine career services in these VET centres that include awareness-raising about entrepreneurial opportunities. Student competition are being implemented to encourage learners to engage in a practical entrepreneurial experience, such as the Youth Business Workshop in VET that started in 2021. Azerbaijan is also working towards fostering non-formal learning, with the adoption in 2020 of a rule to support recognition of skills acquired in non-formal ways.

Moreover, different tools have been developed for entrepreneurial learning, such as a new textbook on entrepreneurship, and the launch of the free online portal tehsilim.edu.az offering different courses on entrepreneurial education and innovation. Entrepreneurship is also promoted among the general population, for instance through annual events (e.g. Youth Entrepreneurs Forums), communication campaigns in various media, and showcasing of good practices: KOBIA recently implemented a programme with GIZ to upgrade business and management skills, which included a study tour in different cities and the involvement of successful entrepreneurs who shared their stories.

Finally, there are several examples of co-operation between higher education institutions and businesses, although limited to Baku. KOBIA has signed memoranda of understanding (MoUs) on co-operation with different universities, such as the Azerbaijan University of Economy, Baku State University, and Azerbaijan Diplomatic Academy (among others). These include non-business faculties, which is a notable progress since 2020. This falls within the SEDS 2022-26 objective to implement professional entrepreneurial learning programmes in co-operation with public, private, and academic sectors.

However, Azerbaijan does not currently have an action plan to support entrepreneurial learning. In that regard, there is no formal national policy partnership clearly defining roles of the different stakeholders involved in entrepreneurial learning policies, resulting in co-ordination challenges. The country's overall progress on entrepreneurial learning has been rather limited since 2020. Entrepreneurial learning remains circumscribed to vocational education, and higher education in some instances – but not beyond economics, management, and education specialities. As a result, not all Azeri students engage in at least one practical entrepreneurial experience. Entrepreneurship is not promoted as a career option in general secondary schools nor non-business faculties.

Moving forward, Azerbaijan should include entrepreneurship key competence in all education levels, implementing relevant support in that regard – developing materials, providing pre- and in-service teacher training on the topic, and including entrepreneurship in career guidance in general education. Entrepreneurship could also be further promoted in non-business academic curricula. Azerbaijan could complement its efforts by fostering the development of an entrepreneurial spirit and mindset among students, beyond the hard skills taught (e.g. business plans). Finally, monitoring and evaluation practices could be improved by enhancing the quality and range of indicators collected.

### *Women's Entrepreneurship*

Women's entrepreneurship is mentioned in the SEDS 2022-26 and in the recently adopted law *On the development of micro, small and medium enterprises*, which is more focused on entrepreneurship, with a

direction on support provision for women-led businesses. However, these documents do not outline concrete measures to support female entrepreneurs since the end of the SME Roadmap in 2020. In terms of institutional framework, while Azerbaijan does not currently have a formal national policy partnership on women's entrepreneurship, KOBIA actively co-operates with the private sector, notably with Azerbaijan women's entrepreneurship development association (*Azərbaycanda Qadın Sahibkarlığının İnkişafı Assosiasiyası,* or AQSiA).

Some initiatives have been implemented to support women entrepreneurs in the country and help them unleash their potential. Women-specific programmes have been launched by both public and private actors, sometimes in co-operation: the *Scale up Accelerator Program*, for instance, is an initiative of AQSiA jointly implemented with KOBIA, the Ministry of Economy, the State Committee on Family, Women and Children Affairs, the US Embassy in Azerbaijan, PASHA Bank and PwC Azerbaijan. The eight-week programme notably aims at equipping women with knowledge and skills in digital transformation, communications, investment rules, and self-development. Information on government support programmes available for women entrepreneurs is available on KOBIA and AQSiA's websites.

Particular progress has been made with regard to support for women entrepreneurs in regions: 17 Women's Resource Centres, created by the State Committee on Issues of Family, Women and Children of the Republic of Azerbaijan, are operating in different cities of the country, providing training and consultancy services to help women start their own business. The Centre in Ganja, for instance, implemented the Women's Leadership Summer School, during which women can learn about the government's support measures available for them and extensive information on how to establish and develop a business.

Moreover, Azerbaijan has initiated some actions to encourage women and girls to go into STEM, fields in which they remain largely under-represented. Support measures include awareness-raising and networking activities, e.g. the Women in STEM festival, where female students can find out more about employment opportunities in large companies and hear speeches and masterclasses from experts; and targeted support, although these remain donor-led (e.g. the UNDP Women and Girls in STEM Mentorship programme).

Despite these various and welcome policy developments, Azerbaijan does not have a comprehensive policy approach to women's entrepreneurship. Provisions in existing policy documents are rather limited and the scatteredness of policy initiatives convolute coordination across stakeholders, as well as monitoring and evaluation of women's entrepreneurship policies in general. Furthermore, while women-only programmes are being developed, women's participation in KOBIA's SME training remains rather low, with only 30% of participants to training being women in 2021. Overall, data on female entrepreneurs appears limited, with no studies on barriers to women's entrepreneurship being regularly conducted.

Moving forward, Azerbaijan should adopt a comprehensive policy approach to women's entrepreneurship, with clearly defined measures, targets, timeframe, task allocation across stakeholders, and monitoring and evaluation. This would help streamline and co-ordinate efforts and assess the concrete impact of the different support measures and programmes. Moreover, Azerbaijan could complement existing efforts by fostering women's participation in KOBIA programmes, tackling persisting gender stereotypes, and developing measures to tackle women's involvement in the informal economy. Finally, improved data collection and the conduction of regular assessments/studies on female entrepreneurs in the country would further allow to identify persisting challenges and developing relevant solutions.

### *SME Skills*

Azerbaijan has achieved considerable progress in the area of SME skills since the last SBA assessment. The SME agency, KOBIA, has developed a network of operators – SME Development Centres, SME Houses, SME Friends – across the Azeri territory, which has led to strong improvements in training provision. The SME Development Centers have been providing courses on a wide range of topics (1600

in 2021), from business law to project management, leadership, and export promotion legislation. Moreover, the establishment of an online video training platform has considerably enhanced outreach (notably to outlying regions), and helped SMEs weather the COVID-19 crisis by granting them access to 180 online training courses – including in digital skills and the green economy.

In an effort to tailor training content to SME needs, KOBIA now uses systematic surveys to collect feedback from participants on the training received. This has been reportedly used to improve courses, and the Agency reports plans to develop additional content based on the remaining identified needs.

As recommended in SMEPI 2020, which highlighted the weak SME skills intelligence available in the country, Azerbaijan has worked to develop a framework for collection and analysis of data on SME skills of both managers and employees. The indicators currently available include insights in such areas as in-house training provided by small firms, and surveys are now conducted to assess the training needs of entrepreneurs (KOBIA, 2022[20]). The latter have been used to inform policy making at the national level.

Building on these recent efforts, monitoring practices and data quality could be further improved. KOBIA currently considers the number of participants and their level of satisfaction when adjusting its training programmes (by e.g. changing trainers/experts, revising materials, or developing new in-demand topics). This approach could be refined by capturing the actual impact of training on skills development and SME performance. Also, the Labour Market Observatory, established in 2019, has begun performing labour market analyses, but skills anticipation exercises remain at a very nascent stage.

Moving forward, Azerbaijan could raise awareness of training available among SMEs and the general population, helping them navigate between the different possibilities. Monitoring and evaluation could be improved by evaluating the skills acquired and the impact of training on SME performance and by improving the quality of data collected and published. Finally, Azerbaijan should consider enhancing skills assessment and anticipation tools, building on the new Labour Market Observatory.

## *Pillar C: Access to finance*

### *Legal and regulatory framework*

The previous SBA assessment noted significant progress in strengthening the legal framework for secured transactions. Since then, there have been no notable reforms in this area, and an assessment of commercial banks on the question of how well the framework for secured transactions works suggests there is room for improvement, especially when it comes to enforcement. For instance, according to a recent survey of 19 commercial banks in the country, banks are relatively satisfied with the scope and creation of securities (more so for immovable than movable assets), but all banks view the enforceability of security rights as not efficient. (EBRD, 2022[21]) Improving enforcement should therefore become a priority, as the system for secured transactions could be compromised if it does not play its critical role as the last step of the chain.

The Central Bank of Azerbaijan has managed to improve its regulatory and supervisory framework following major turmoil in the sector in 2015-16, and continuity of policies assisting the emerging credit growth will be important in order to cement an environment for healthy financial development. Basel III principles are being introduced and implemented and the Central Bank has moved toward an enhanced risk-based supervision and stress-testing model. Currently, however, non-financial disclosure requirements for banks relate only to corporate governance standards and do not take into account environmental or social aspects. There is also no climate-related stress testing or green taxonomy. These are areas of increasing importance that should be incorporated into a forward-looking supervisory approach. The Central Bank has worked with IFIs and experts on developing its first Sustainable Finance Roadmap, which is an important step in this direction.

As of March 2023, deposit dollarisation remained high at 46%, which may constrain the sector's ability to extend local currency loans in the longer term. Nevertheless, foreign currency lending has declined, with only 10% of new loans and around 20% of banks' loan portfolios denominated in foreign currency. Regulatory provisions that encourage local currency lending, such as higher capital requirements and risk weights for foreign currency loans and mandatory disclosure of the risks of FX borrowing, have supported this trend.

The banking sector is quite concentrated, with the assets of the top four banks representing around 68% of total banking assets as of June 2023. This share has increased since the last assessment in 2019. Greater support to smaller banks with a more pronounced SME focus and strategies, including FDI, would be helpful in fostering competition which in turn could encourage greater supply of finance to SMEs.

The Baku Stock Exchange has a premium and a standard segment with a total of 24 stocks and 254 bonds issued. Issuances, especially in the premium segment, are dominated by state-owned entities, whereas in the standard segment, a majority of issuers of both stocks and bonds are financial institutions with only a limited number of corporates present.

### *Sources of external finance for SMEs (bank financing, non-banking financing, and venture capital)*

Following a slow recovery from the 2015-16 crisis, Azerbaijan went through a double shock from reduced demand for oil coupled with a decline in economic activity due to measures against the COVID pandemic in 2020. In this environment, new lending was largely suspended in the country and the sector embarked on a major loan restructuring, reaching around 12% of the sector's gross loan portfolio. In addition, the licenses of four banks with long-standing solvency issues were withdrawn in 2020, largely completing a major sector clean-up since 2015-16. The government stepped in with a significant support package for real sector borrowers and the Central Bank introduced several regulatory changes to ease pressure on banks on a temporary basis (now fully phased out).

After a low in December 2020, lending recovered with positive credit growth year-on-year. Since the last assessment, the share of SME loans in total loans has steadily increased, from around 42% in 2019 to 51% in the first half of 2022. Around 12-14% of SME lending has been publicly supported (Central Bank of the Republic of Azerbaijan, 2022[22]). This means that access to finance has eased overall, which is also reflected in results from an enterprise survey conducted in 2019 where 26% of SMEs identified access to finance as an obstacle to doing business, compared with 34% in 2014 and 50% in 2009. For those businesses needing a loan but not able to access one, the main reasons were high interest rates and collateral requirements (EBRD, 2020[23]).

Support programmes were expanded during the pandemic and are mainly provided through the Entrepreneurship Development Fund, which issues guarantees and subsidised loans. In 2022, 2 726 soft loans were disbursed through the Fund, the vast majority of which went to SMEs (see Box 11.1). Although there is an annual audit report on the Fund's activities, there does not seem to be a separate, formal impact evaluation mechanism and no channel through which private banks can provide feedback. Applications are open to businesses in the non-oil sector and certain investments are identified as a priority, such as projects related to, for example, innovation, digitalisation, greening and tourism.

When it comes to non-bank financing, SMEs can access microfinance, leasing and factoring opportunities, but these sources remain underdeveloped. A clear picture is difficult to establish in the absence of reliable data, however. A new Strategy for Financial Inclusion is currently being drafted which should provide a more supportive legal framework for microfinance by allowing MFIs to provide auxiliary services and by expanding payment options for micro loans. Leasing and factoring are available through some banks, but leasing activities are not regulated, and uncertainty in the legal framework around the definition of different types of factoring hinders the wider development of this instrument. Work on a draft law on leasing is

currently being carried out, and a review of factoring legislation (with a view to enabling supply-chain finance and easing the use of movable assets as collateral) is underway. These efforts will be crucial to bring both sectors onto a more promising footing and provide SMEs with much-needed alternatives to bank financing.

Due to a missing legislative framework, venture capital remains nascent and until recently there was not much investment activity. However, in November 2023 the first local venture fund, “Caucasus Ventures”,was established with paid-in capital by the Innovation and Digital Development Agency, PASHA Holding, and local entrepreneurs, amounting to AZN 11.3 million (EUR ~6.3 mln). The plan is to invest these funds in around 50 projects in Azerbaijan and the wider region over the coming five years. So far, three investments have been made, and it is too early to tell whether this fund could act as a catalyst for the sector. For earlier-stage investments, grants and accelerator support from the Innovation Agency are available, but information about support opportunities is not easy to access, and funding beyond the very initial stages is difficult to get. No business angel network exists, either, which means that start-up funding, in particular from private investors, is very scarce.

### *Financial literacy*

The Central Bank conducts annual financial literacy surveys to gauge the level of financial literacy in the population. This is an important foundation for formulating policy responses to improve financial literacy. Following on the previous Financial Literacy Strategy in 2016, Central Bank is currently preparing a new strategy with the aim of adoption it by end 2023. In recent years, a number of resources have been made available to enhance the understanding of the population, including entrepreneurs specifically. A general financial literacy portal (bizimpullar.az) provides access to news and basic information around finance and monetary policy. In 2022, the portal was accessed by 30,957 visitors. It is complemented by a training platform (edu.e-cbar.az) offering online courses on more in-depth topics such as capital markets, how insurance works, digital financial literacy, etc. In addition, an information platform (infobank.az) provides information around different types of financial instruments that people can access and attracted 14,007 visitors in 2022. These resources cater to both the general population as well as entrepreneurs. Monitoring of usage is useful to gauge whether the offer corresponds to what people need or expect, but the Central Bank should consider more rigorous evaluations of its programmes and how they translate into better financial literacy among the population in order to establish a clear link between the policy efforts made and the outcomes measured in its annual surveys.

### *Digital financial services*

In 2023, the Central Bank prepared a Digital Payments Strategy which covers aspects of digital financial service regulation. It is centred around 5 pillars: (i) improvement in legislation to support digital payment provision, (ii) expansion of coverage, (iii) development of risk-based regulation, (iv) increase in financial inclusion, and (v) improvement in financial literacy. All of these aspects can also support the development of digital financial services more generally. The development of digital payments and their outreach is also supported by the International Finance Corporation (IFC) in co-operation with Swiss and German donors. (IFC, 2021[24])

Several stakeholders are involved in discussions around digital financial services, such as the Central Bank as well as the Azerbaijan Banking Association. There seems to be no multi-disciplinary task force that brings together representatives from different branches of government and the private sector to discuss and decide on regulatory approaches to digital financial services. Having such an institution in place is particularly important in the context of digital financial services given that they span across spheres of activity that require solutions from different disciplines.

Provisions on data protection and rules around data sharing are in place. However, outsourcing provisions are not yet fully regulated, meaning there is currently no requirement for or limit on, for instance, banks

outsourcing even core services. The application of a wider toolbox (e.g. . suptech[4] application, regulatory sandbox, central bank digital currency) by the Central Bank is still at a nascent stage, but some preparatory work is underway.

#### *The way forward*

Moving forward, Azerbaijan should improve the legal framework for secured transactions by facilitating the use of movable assets as collateral and strengthening the system for enforcement. This would require a wider review of legislation as well as enforcement mechanisms, both in and out of court. A lengthy and difficult enforcement process makes banks more reluctant to lend to SMEs at reasonable rates, and heavy reliance on immovable assets reduces funding opportunities for asset-light businesses, many of which tend to be SMEs.

In addition, the country should deepen financial inclusion by supporting the development of non-bank financing options. The adoption of the new financial inclusion strategy as well as the new law on leasing would be an important step in this direction. These instruments need to become viable financing options for SMEs in order to give entrepreneurs the ability to choose the t instruments best suited to their individual needs and situations. The available information platforms are already a good tool for raising awareness, but now policy attention should focus on making these options usable.

The scope and depth of statistics on access to finance for SMEs should be further improved, especially with regard to non-bank funding sources, where no statistics are currently publicly available. These statistics will allow important for the government to (a) formulate effective and targeted policy responses and (b) monitor whether policy changes have an impact on financial outcomes. Making the statistics public, meanwhile, would mean they can also become an important information source for financial service providers working to develop new product offerings that are tailored to the needs of SMEs in the country.

Across the board, policies should focus on bringing in private funding and investment instead of using public sources. For example, while the newly established venture fund has the potential to improve the financing environment for start-ups, more policies are required that leverage private money and create an environment in which private investors are able to operate in the country.

### *Pillar D: Access to markets*

#### *Public procurement*

Since the latest assessment, some successive adjustments of details in the legal framework as well as enhancements to the e-procurement system have been made, while principles and practices have seen little change.

The public procurement law (PPL) of 27 December 2001 remains in force. It applies to all kinds of entities financed from the state budget or owned by the state. Significant amendments were made on 28 December 2018, introducing general regulations for e-procurement as well as integrity requirements and other provisions intended to support SME participation. Several subsequent amendments have been made to add clarity and adjust the tender security threshold. The PPL is complemented by presidential decrees, decisions by the Cabinet of Ministers and other legal acts on the implementation of the PPL. However, the PPL is not set in any wider policy context, in the form of a medium-term programme for the development of public procurement or the like.

The institutional framework is unchanged. All central public procurement functions, including the review of complaints, remain assigned to the State Procurement Control Department (SPCD) of the State Service for Antimonopoly Policy and Consumer Protection under the Ministry of Economy. The SPCD runs the e-procurement system. Its main features cover publication of notices and reports, distribution of tender documents, submission of tenders, and evaluation, including in the form of electronic auctions. The PPL

allows award criteria other than price to be used but this is rare in practice, especially since any tenders above the estimated cost (which is supposed to be kept secret) will be automatically rejected. The PPL requires contracting authorities to set up ad-hoc “tender commissions”, but without any requirement to have properly staffed, dedicated procurement units. This is intended to help involve specialists from all other relevant fields in the process but may limit the scope for enhanced professionalisation.

The PPL provisions intended to support SME participation include obligations for timely payments, the possibility of division into lots, and a general requirement for all contracts with an estimated value up to USD 3 million to be procured using the e-procurement system, with participation limited to SMEs. If subcontracting is envisaged, it is also required to reserve at least 20% of the value of the subcontracts for local SMEs. On the other hand, other features are still likely to discourage SME participation, including unclear and incomplete provisions on grounds for exclusion and qualification requirements and onerous documentation requirements for demonstrating compliance, fees for accessing tender documents, and obligations to provide tender securities and contract execution guarantees. A further disincentive is that the sequence of e-procurement steps allows the participation of unqualified tenderers with tenders that do not match the requirements.

Some data on public procurement can be extracted from the e-procurement system – essentially for contracts below USD 3 million, where its use is compulsory. However, the data available is hardly sufficient for analysing the various features that may support or discourage SME participation in public procurement: such an analysis is needed in order to determine the mechanisms at play and their effects and thus create an evidence base for reform.

Moving forward would therefore require meeting the following challenges, among others: i) setting the PPL in a wider, medium-term policy context, harmonised with other policies (e.g. for SME support and for sustainable development) and updating it accordingly; ii) revising the institutional framework in order to reduce conflicts of roles and raise the level of professionalism; and iii) expanding the use of the e-procurement system, adjusting the sequence of steps, and ensuring that data on all public procurement is collected and made accessible.

### *Standards and technical regulations*

Regarding overall co-ordination and general measures, Azerbaijan has made progress in aligning its national legislation with WTO requirements through various legislative amendments (Ministry of Economy of the Republic of Azerbaijan, n.d.[25]). New laws on standardisation and technical regulation have aligned country with international requirements. The Law “On Technical Regulation” (No. 1669-VQ, dated 30 September 2019) determines mandatory requirements for goods, processes, production methods, and conformity assessment. In this context, it also aims to stimulate the activities of accredited certification bodies. The relationship between Azeri conformity-assessment legislation and the EU *acquis* is described in the relevant section below.

Regarding market control, the State Service for Antimonopoly and Consumer Market Control was integrated into the structure of the Ministry of Economy with the status of a relevant public service by Decree 845 in 2019. The Decree also specifies the "Azerbaijan Standardisation Institute" (AZSTAND) as a public legal entity belonging to the State Service Antimonopoly and Consumer Market Control. Several market surveillance measures are already in place, and others are being developed. Current Azeri legislation associates "market surveillance" mainly with inspections, but various market monitoring activities have also taken place. Businesses involved in export can obtain all the required certificates from the "One Stop Shop" Export Support Centre. In addition, the Azexport platform (Azexport.az) provides information on Azeri products to support their foreign sales. Action items include the further development of market surveillance and the regular evaluation of the quality infrastructure.

With regard to harmonisation with the EU *acquis*, Azerbaijan continues using twinning projects[5] for various societal issues, including standardisation (European Commission, 2020[26]). With German support, the

country has implemented a National Plan for harmonizing its standardisation system with international requirements (EU-Azerbaijan Business Forum, 2021[27]), and the adoption of EU standards has begun. In 2023, the State Program "On the harmonization of the national standardization system in accordance with international requirements for 2023-2025" was approved. It provides for the adoption of about 90 technical regulations based on European directives and regulations, as well as the adoption of about 7,000 reference standards. Legislation on accreditation and conformity assessment does yet not align with the EU *acquis*; these are still barriers to the Azeri-EU trade.

Regarding SMEs' access to standardisation, Azerbaijan initiated more than 70 training events in 2022. Likewise, financial support for acquiring standards is available. An action plan to improve education about standardisation does not exist yet, but a recent collaboration agreement between AZSTAND and the State Oil and Industry University could be a starting point for further action.

Concerning the digitalisation of standards and technical regulations, in 2023 AZSTAND introduced a standards document management system and an electronic sales platform. Likewise, Azerbaijan has a plan for digitising its metrology institute. The further digitalisation of the country's quality infrastructure should also include a strategy or action plan for digitising the national accreditation body. Overall, Azerbaijan's development indicates that the country's quality infrastructure will continue progressing. An intensification of its relations with the EU *acquis* is also evident.

### *Internationalisation of SMEs*

Azerbaijan has achieved limited progress in supporting SME internationalisation since the last SBA assessment.

Export diversification has always been a priority on the government’s agenda. Although the new export strategy is yet to be approved, “Diversifying and supporting growth of non-hydrocarbon exports” is one of the main directions outlined in the Implementation Plan of the 2022-2026 Socio-Economic Development Strategy of Azerbaijan. Targeted support for SMEs to enhance their export capacity is also covered by the direction on “Improving SME access to resources, including finance”.

The country’s export and investment promotion agency, AZPROMO, remains the main institution in charge of export promotion services. The agency was established in 2003 by the Ministry of Economy to attract foreign investment in the non-oil sector and encourage exports of non-oil products. To this end, it organises various international events to raise awareness of Azerbaijani products among foreign consumers and to promote them in foreign markets. AZPROMO is also tasked with the promotion of the “Made in Azerbaijan” brand (AZPROMO, 2023[28]). This brand was established by a Presidential Decree, which provides for ten different support mechanisms financed by the state budget and available to exporters. The support mechanisms include export missions, organisation of buyer missions to Azerbaijan, market research, and participation in international exhibitions and fairs at a single country stand. KOBIA also provides a number of services to help SMEs access international markets, mostly in the form of support for SME participation in exhibitions. However, as was also the case for the last SBA assessment, these support mechanisms are mostly focussed on facilitating companies’ participation in international trade fairs and the organisation of trade missions, and there seems to be no financial support mechanism available that systematically supports exporting SMEs across the sectors or provides trade insurance services.

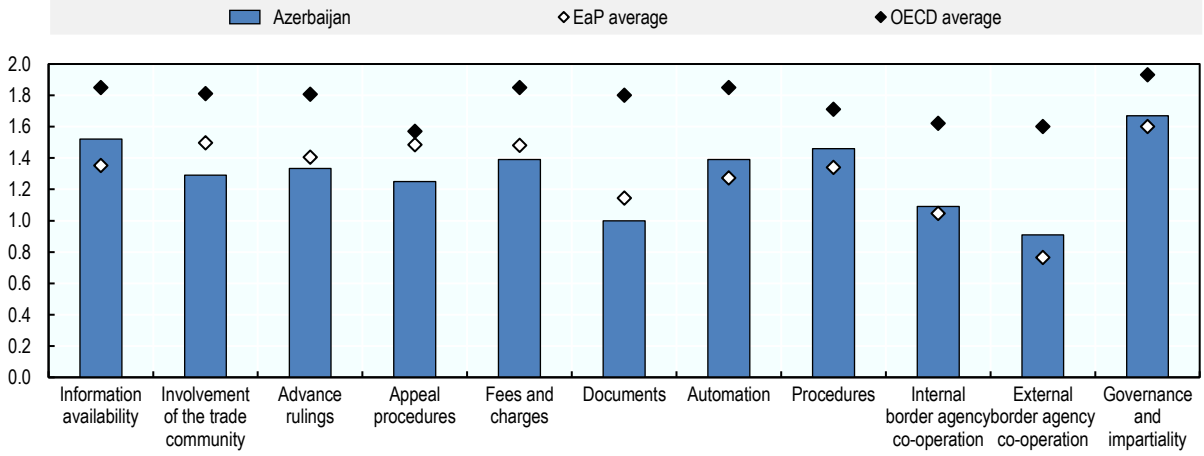
Promotion of the use of e-commerce is also among the objectives of the 2022-2026 Socio-Economic Development Strategy, and its Implementation Plan includes many activities in this regard, including “Improve the e-commerce legal framework (address barriers) and promote reduction of illegal trade”. Currently, the regulatory framework is defined by the Law on E-Commerce and the Law on Electronic Signature and Electronic Document. In terms of direct support for businesses, Azerbaijan is promoting cross-border digital trade through partnerships with some of the world’s largest e-commerce companies under the Azexport platform (azexport.az), managed by CAERC. In 2021, KOBIA also established an online sales platform specifically targeted at SMEs (kobmarket.az) to help them expand their customer

bases and move their businesses online (OECD, 2022[29]). However, there seems to be no comprehensive legal framework for online consumer protection. Nevertheless, the main barriers to the development of e-commerce among SMEs seems to be connected to framework conditions for digitalisation, such as limited access to computers and to affordable and high-quality Internet connection, and low level of digital skills (see under "Digital skills" earlier in this chapter). To conclude, it is also worth mentioning the eCommerce pilot between Armenia, Azerbaijan, Georgia and Germany launched in 2021 by EU4Digital to establish national virtual warehouses/databases of local goods to connect eCommerce actors so they can automatically exchange information about sales, customs and delivery (EU4Digital, 2021[30]).

Although the government does not carry out regular assessments of the changing global value chains (GVCs) to understand the main opportunities for SMEs, and while there are no comprehensive and structured programmes to promote SME integration into GVCs, KOBIA should support the creation of SME clusters. A dedicated support mechanism was established in 2022 by Presidential Decree No. 1905 whereby eligible SMEs can apply to obtain substantial exemptions from various classes of taxes for seven years. The exemptions concern profit tax, land tax, property tax, income tax, and a VAT exemption on the import of machinery, technological equipment, and devices for production or processing purposes. However, the tax concessions are not yet being applied, pending detailed regulations from the Ministry of Economy and the Tax Administration.

According to the 2022 OECD Trade Facilitation Indicators, Azerbaijan's performance is, on average, in line with that of other EaP countries. However, the country still lags behind OECD members across all areas assessed, and significant challenges remain. Azerbaijan should focus on improving automated procedures (e.g. electronic exchange of data and use of automated risk management), streamlining border control procedures (e.g. inspections, clearance), and implementing trade single windows and certified-trader programmes. Furthermore, the number and diversity of fees and charges collected could be reduced (see Figure 11.5).

## Figure 11.5. OECD Trade Facilitation Indicators for Azerbaijan (2022)




Note: TFIs take values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade Facilitation Indicators Database, https://oe.cd/tfi.

StatLink https://stat.link/lry73b

Overall, efforts to monitor and evaluate existing programmes and supporting mechanisms to promote SMEs' access to international markets are extremely limited. The government should also improve the design of the promotion programmes by attaching measurable targets directly to these initiatives, rather than to the relevant policy strategy. Azerbaijan should prioritise the approval of the new Export Strategy

and expand export promotion among SMEs by introducing a financial support mechanism that systematically supports exporting SMEs across the sectors and provides trade insurance services. To promote the use of e-commerce among SMEs, Azerbaijan should strengthen the legal framework for online consumer protection as well as framework conditions for digitalisation. Finally, Azerbaijan should implement the planned cluster tax concessions to expand support for SME integration into GVCs.

### *Pillar E: Innovation and business support*

#### *Support services for SMEs and start-ups*

Following the SME Road Map 2016-2020, no dedicated SME Strategy or equivalent policy document with an exclusive focus on SMEs has been adopted by the government. Instead, some provisions on a range of SME-related policies can be found in the Socio-Economic Development Strategy 2022-2026, including on entrepreneurship, financing, and innovation. Its action plan, however, remains rather high-level, with few details and no indication of costing of individual measures.

The Small and Medium Business Development Agency ("KOBIA"), operating under the Ministry of Economy, is the main government body co-ordinating the provision of business support services to SMEs and start-ups. Since the latest SBA assessment, the agency has rolled out its network of sub-structures to ensure outreach to SMEs throughout the country: i) three SME Houses (in Baku, Khachmaz and Yevlakh) serve as local one-stop-shops for entrepreneurs providing over 150 governmental services from 29 state institutions; ii) 21 SME Development Centers provide a wide range of services to start-ups and entrepreneurs, with a focus on training and consulting to establish and develop their business; and iii) 45 SME Friends, liaising directly with entrepreneurs and business associations to increase awareness about available government support programmes.

KOBIA's model to support the SME community in Azerbaijan is to provide services that are free of charge for its beneficiaries. Through the SME Development Centers, SMEs can easily attend trainings on a wide range of business-related topics (from strategic planning to business ethics) and request consulting support from advisors pre-selected by KOBIA. According to information provided by the government, in 2021 more than 700 training sessions were conducted and over 11 000 hours of consulting services delivered for a total of nearly 10 000 beneficiaries. In addition, KOBIA directly performs market studies, both on its own initiative and upon specific requests from SMEs.

Overall, while this approach may have helped to broaden SME access to general market information, educational opportunities and advisory services, public support for SMEs to access tailored advice and specialised expertise from external consultants of their choice is less developed. Entrepreneurs in Azerbaijan can apply to KOBIA's grant competitions (up to EUR ~11 000) and, if successful, can use the funds to cover expenses in various areas, from expanding production facilities to procuring consulting services. In practice, however, the number of beneficiaries remains small (39 grants awarded since the inception of the programme in late 2020). Furthermore, the lack of a cost-sharing mechanism for receiving business advisory services provided by the SME Development Centers may lead to an "over-consumption" by SMEs, and the fact that the advice itself is delivered by staff of the Centers does not open up opportunities for external consultants who may be better placed to provide specialised expertise.

Specifically, to support SME digitalisation, KOBIA has done some initial analysis on the ICT needs of SMEs and offers in-person session and online videos as part of its wide offer of trainings. [6] The "one-to-many" nature of these trainings, however, falls short of matching good practices where individualized assessment and company-specific digitalisation roadmaps are developed with the support of specialised consultants.

Lastly, Azerbaijan has made marginal progress in the area of monitoring and evaluation. The Center for Analysis and Communication of Economic Reforms is tasked with monitoring the Socio-Economic Development Strategy 2022-2026 and the progress towards its targets, based on the information received from implementing agencies. For specific SME support programmes and initiatives, however, monitoring

remains focused on take-up – i.e. the number of participants in training events and, in some cases, surveys of user satisfaction – and lacks a rigorous evaluation of the impact of the support on beneficiaries' business performance.

Moving forward, building on the information included in the general Socio-Economic Development Strategy, the government could consider developing a separate strategic document or action plan on SME-related activities, including an indication of detailed costing, which would incorporate a sharper SME angle into the broader national economic policymaking. Further, KOBIA could facilitate access to external consultants who can provide specialised advice to SMEs on topics of their choice (ongoing initiatives such as EBRD's Advice for Small Businesses programme are a useful reference in this regard). Existing elements that support SME digitalisation could also be strengthened and brought together through a dedicated programme for SME digitalisation, which would offer entrepreneurs an analysis of their needs, company-specific digitalisation roadmaps, and dedicated financial support tools to implement them. Lastly, while monitoring activities are routinely implemented at different levels, the evaluation of SME policies could be taken to the next level with a pilot project designed to rigorously assess the impact of selected support programmes on beneficiaries' performance.

### *Innovation policy for SMEs*

No dedicated national innovation strategy currently exists in Azerbaijan. The Socio-Economic Development Strategy 2022-2026 does include (in the section "National Priority 3. Competitive Human Capital and Modern Innovations Space") ambitious measures to develop the innovation ecosystem and stimulate innovation in the business sector, some of which are clearly relevant for start-ups and SMEs. Many activities in the action plan, however, contain few implementation details and lack an indication of the costs foreseen.

The establishment, in October 2021, of the Innovation and Digital Development Agency (IDDA, under the Ministry of Digital Development and Transport) is the most relevant development on the institutional framework for SME innovation since the previous SBA assessment. As the product of a merger of three previously existing bodies (the National Nuclear Research Centre, the Innovation Agency, and the High Technologies Research Centre), the agency's mandate is rather broad. Its objectives include building a digital government and society, carrying out nuclear research, supporting technology upgrades and innovation-oriented research by businesses, and promoting the competitiveness of the IT sector. Several other government agencies are involved in supporting innovation in Azerbaijan, in particular the aforementioned Centre for Analysis and Coordination of the Fourth Industrial Revolution (an advisory body promoting international co-operation), KOBIA (the SME agency), and the Agrarian Science and Innovation Centre (focused on innovation in the agriculture sector).

Physical infrastructure for innovation in Azerbaijan features technology parks (or "technoparks"), such as the Sumgait Chemical Industrial Park and the Azerbaijan National Academy of Sciences (ANAS) High-Tech Park. It also has a growing number of incubators and accelerators (e.g. Innoland, SABAH.lab), driven by both public and private initiatives. While the former provides their resident companies with logistical infrastructure and a range of tax concessions and exemptions related to innovation activities (e.g. VAT and customs fee exemptions on equipment to carry out R&D) for up to 10 years, the latter support business creation and innovative start-ups with co-working facilities, training, and networking opportunities. Even though information on the state of its implementation is not available at the time of writing (June 2023), it is also worth mentioning here the government's ambitious plan to develop the innovation ecosystem with the creation of Absheron Valley, a cluster with innovation and acceleration facilities with the goal of hosting over 300 start-ups by 2026.

Available financial instruments to support innovation in Azerbaijan have also undergone some changes. The most important development is the introduction of the so-called "Startup Certificate", a scheme through which micro and small businesses can benefit from a tax exemption on the profits generated by the sale

of innovative products or services for a period of three years. Moreover, a new package to incentivise investment in the IT sector (software development and system integration) was approved in January 2023, cutting profit and income taxes for both companies and their employees qualifying as residents of technoparks. Lastly, science-, research- and innovation-oriented projects are also eligible for the grant competitions administered by KOBIA described in the previous section. Overall, Azerbaijan's incentives for innovation by businesses continue to be focused on the start-up segment and the IT sector – whereas broad, indirect financial incentives for innovation and research and development (R&D) for the larger SME population remain unavailable.

Azerbaijan's monitoring and evaluation practices for innovation support are broadly aligned with those for general business support services, and they remain focused on programme take-up (e.g. 94 start-up certificates were issued in the period between May 2021 and May 2023) rather than on the impact of such instruments on actual innovation performance. However, Azerbaijan's statistical office produces accurate information on SMEs' expenditure on R&D, broken down by enterprise size class, which is a rare and welcome step towards equipping the government with outcome-oriented indicators for its innovation policy efforts.

### *SMEs in a green economy*

Azerbaijan's SEDS 2022-26 includes a chapter on promoting a "clean environment and green growth country", which calls for environmentally friendly industrialisation and includes broad targets related to waste management, biodiversity, aquaculture, land preservation, renewable energy, and energy efficiency. However, there are no specific references to actions targeting SMEs and it is not clear what role SMEs will play in supporting the achievement of the intended targets. Furthermore, the existence of strong subsidies on energy tariffs for end users reduces the incentives to adopt energy-efficient technologies for both businesses and households (IEA, 2023[31]).

Many of the sectors targeted, including agriculture and aquaculture, have a significant SME presence and would benefit from implementation plans adapted to enterprise size and capabilities. Overall, Azerbaijan lacks a focus on supporting green SMEs, or green enterprises more broadly, beyond those involved in the green energy sector, and the SME development agency would be ideally positioned to reach out to SMEs and provide information on the benefits of adopting resource-efficient practices.

Although some regulatory and financial instruments for promoting greening practices among SMEs have started to become available in Azerbaijan, they remain small-scale. The 23 enterprises operating in the Balakhani eco-Industrial Park, for instance, are specifically involved in waste recycling and the production of "green" products, and as such can benefit from profit, land and property tax exemptions for a period of 10 years. On the financing side, the state-owned Entrepreneurship Development Fund provides soft loans to local SMEs and since 2021 has considered ESG criteria in its financing decisions. On the monitoring side, the lack of SME greening-specific policies and instruments makes it difficult to assess the impact of environmental policies on the SME sector.

Moving forward, Azerbaijan could leverage the strong reach of the SME development agency to promote resource-efficient practices among SMEs, develop regulatory and financial incentives for greening practices beyond the energy sector, and strengthen monitoring tools that specifically address SMEs' environmental performance.

## The way forward

Azerbaijan's government continues to make efforts to foster the development of the SME sector, with a view to supporting economic diversification. Moving forward, the government should consider the following measures:

- Azerbaijan's government should ensure the upcoming NDS adopts a comprehensive approach for digital transformation in non-IT sectors (particularly SMEs), sets clear objectives, allocates resources, defines targets, and establishes process- and result-oriented indicators. To enhance impact, a multi-stakeholder approach should be pursued, building on the newly established working group and involving private sector representatives to ensure diverse perspectives. Collecting additional data aligned with EU and OECD methodologies would enable better policy assessment and international comparison. Efforts should also be directed towards improving high-speed Internet access, by lowering barriers to broadband access via conducive regulations and improving communication network resilience. As for digital skills, Azerbaijan should strengthen skills assessment and anticipation tools, adopt a digital competence framework, and provide widespread digital skills training opportunities across the country.
- To improve the institutional framework and operational environment for SMEs, Azerbaijan needs to continue building on achievements from the 2016-2020 SME Road Map. A comprehensive strategy for SMEs should be integrated into the broader National Socio-Economic Development Strategy, ensuring that co-ordinated policies are aligned with wider economic objectives. Optimal SME policy necessitates stakeholder co-ordination, regulatory impact assessment (RIA), business licensing simplification, and fostering public-private discussions via platforms like the Public Council. The operational environment should be prioritised, ensuring accessible e-servicesand reduced administrative complexity as well as enhancement of digital government services and maintenance of streamlined company registration processes. Simplifying tax compliance, while also incorporating SME-friendly exemptions and reductions, is pivotal. Enhancing the bankruptcy framework involves considering the introduction of simplified processes for small cases or SMEs, introducing early warning systems, and establishing mechanisms to promote second chance for honest entrepreneurs.
- On entrepreneurial learning, Azerbaijan should incorporate entrepreneurship as a key competence across education levels, offering support through materials, teacher training, and career guidance. More efforts could be provided to help individuals develop an entrepreneurial mindset, beyond hard skills. As regards women's entrepreneurship, Azerbaijan should adopt a holistic policy that features well-defined measures, targets, and timelines. This approach would facilitate co-ordinated efforts, allowing for effective monitoring and evaluation of diverse support measures. Efforts should be made to integrate women into KOBIA programmes, countering gender stereotypes and women's informal economy participation. Overall, enhancing the quality and scope of indicators for monitoring and evaluation for both entrepreneurial learning and women's entrepreneurship is essential to track progress; this should be complemented by regular assessments/studies on female entrepreneurs to provide insights into persistent challenges and guide the development of appropriate solutions. Building on the considerable progress recently achieved in terms of support for SME skills development, Azerbaijan should increase awareness about available training options for SMEs and the public, alongside enhancing the monitoring and evaluation of training outcomes. Skills assessment and anticipation tools could be developed, building on the new Labour Market Observatory.
- Azerbaijan needs to enhance its legal framework for secure transactions by simplifying the use of movable assets as collateral and strengthening enforcement systems. This will encourage banks to lend to SMEs at fair rates. Moreover, promoting non-bank financing options will deepen financial inclusion. These options should become viable for SMEs, offering tailored choices. While existing information platforms raise awareness, policy focus should shift to usability. Improving SME finance statistics is crucial – especially for non-bank funding, which currently lacks publicly accessible data. These statistics would help the government formulate effective policies and monitor their impact, while also guiding providers to design and offer tailored financial products. Policy emphasis should be on attracting private investment rather than replacing it with public funds. Although the

established venture fund aids start-up financing, more policies are needed to attract private investors and foster a conducive operational environment.

- Azerbaijan should improve the business environment by aligning standards and technical regulations with broader policies like SME support and sustainable development, harmonising legislation and policies effectively. This involves updating laws for better international alignment and clarity. To bolster professionalism and streamline processes in public procurement, the institutional framework should be revised and dedicated procurement units established in contracting authorities. Azerbaijan should expand the use of e-procurement with a revised sequence of steps, while ensuring comprehensive data collection and accessibility. Promoting SME participation in public procurement should entail reviewing and simplifying regulations, reducing fees, and ensuring fair competition. Developing comprehensive digitalisation strategies, including plans for digitising the national accreditation body, will enhance the quality infrastructure. Facilitating SME internationalisation necessitates the introduction of a financial support mechanism that systematically supports exporting SMEs and the provision of trade insurance services, the reinforcement of the legal framework for online consumer protection as well as framework conditions for digitalisation to expand use of e-commerce, and the implementation of the planned cluster tax concessions to expand support for SME integration into GVCs. Trade facilitation processes should be improved via automation and reduced fees.
- The government could consider developing a separate strategic document or action plan on SME-related activities, including an indication of detailed costing, which would incorporate a sharper SME angle in the broader national economic policymaking. Further, KOBIA could facilitate access to external consultants who can provide specialised advice to SMEs on topics of their choice. Existing elements that support SME digitalisation could also be strengthened and brought together through a dedicated programme for SME digitalisation. Lastly, the evaluation of SME policies could be taken to the next level to rigorously assess the impact of selected support programmes on beneficiaries' performance. To enhance Azerbaijan's innovation landscape, the physical infrastructure for innovation could be expanded by bolstering technology parks, incubators, and accelerators, while actively realizing the vision of the Absheron Valley. Financial instruments, including the "Startup Certificate", could be extended and supplemented with broader incentives for innovation and R&D, benefiting a wider range of SMEs beyond the IT sector. To foster eco-friendly growth in Azerbaijan, SME involvement should be explicitly incorporated into targeted actions for green initiatives and aligned with environmental goals. Implementation plans for SMEs, especially in sectors like agriculture and aquaculture, should be adapted to the practices of their size and capabilities. Beyond green SME support for energy, Azerbaijan should extend support to other sectors, leveraging the SME agency for resource-efficient practice dissemination. In addition, regulatory and financial incentives should be strengthened, building upon models like Balakhani Industrial Park to encompass a wider range of businesses.

### Table 11.5. Roadmap for policy reforms – Azerbaijan

| |
|---|
| **Strengthening framework conditions for the digital transformation** |
| • Adopt a comprehensive NDS, including provisions for the digital transformation of non-IT sectors |
| • Ensure co-ordination across public and private stakeholders throughout implementation. |
| • Enhance data collection aligned with EU and OECD methodologies to facilitate policy assessment and international benchmarking. |
| • Focus on improving high-speed Internet accessibility by lowering barriers to broadband access through regulation and policies to enable investment, while safeguarding competition, investment incentives and enhancing communication network resilience. |
| • Improve digital literacy by strengthening skills assessment and anticipation tools, adopting a digital competence framework, providing digital skills training across the country, and fostering a multi-stakeholder approach for digital skills policies. |
| **Enhancing the institutional and regulatory framework and operational environment for SMEs** |
| • Ensure timely implementation of SME policies from the Socio-Economic Development Strategy via monitored action plans, supported by annual SME development report in collaboration with KOBIA. |

- Hold regular public-private consultations involving the Ministry of Economy, KOBIA, and SME representatives. Review strategy progress and adapt to economic conditions.
- Enhance RIA method per global standards, applying it broadly to new laws for better impact assessment.
- Finalise the Digital Economic Strategy, aligning it with Digital Azerbaijan Project and e-government services.
- Enhance inter-agency co-ordination, unify the e-government platform, and bolster data base interoperability.
- Track SMEs' e-government service adoption and educate non-users about options for accessing digital government services.
- Establish robust monitoring for new tax incentives from Start-up and Cluster Enterprises laws.
- Strengthen bankruptcy procedures with streamlined options for small cases or SMEs, implementing early warning systems and establishing policies to promote second chances for honest entrepreneurs.

**Promoting entrepreneurial skills and women entrepreneurship development**

- Integrate entrepreneurship as key competence in education at all levels, accompanied by relevant support measures.
- Further promote entrepreneurship in non-business academic curricula.
- Cultivate an entrepreneurial spirit among students, complementing hard skills with practical entrepreneurial experiences.
- Enhance data collection and perform regular studies on entrepreneurial learning and female entrepreneurs.
- Adopt a comprehensive policy for women's entrepreneurship with clear measures, targets, timelines, and monitoring and evaluation.
- Promote women's participation in KOBIA support programmes.
- Tackle persisting gender stereotypes and women's involvement in the informal economy.
- Raise awareness of training available among SMEs and the general population, helping them navigate the different options.
- Enhance monitoring and evaluation by assessing impact of training programmes and skills acquired, and by improving data quality.
- Develop skills assessment and anticipation tools, building on the new Labour Market Observatory.

**Facilitating SME access to finance**

- Enhance the legal framework for secured transactions by simplifying the use of movable assets as collateral and strengthening enforcement systems.
- Promote financial inclusion through non-bank financing options by implementing new financial inclusion strategy and leasing law, ensuring SMEs with tailored viable choices.
- Strengthen SME finance statistics, especially on non-bank sources, for better policymaking, monitoring, and product development.
- Attract private funding and investment in the SME and start-up sector, leveraging the venture fund.

**Supporting SME access to markets**

- Align standards and technical regulations with broader policies like SME support and sustainable development, refining laws to meet international requirements and ensure clarity.
- Enhance efficiency and professionalism of public procurement by establishing dedicated procurement units in contracting authorities.
- Extend e-procurement use, improving data collection, and ensuring comprehensive data accessibility for public procurement.
- Encourage SME participation in procurement by simplifying documentation, reducing fees, and ensuring fair e-competition.
- Develop comprehensive digitalisation strategies, including the accreditation body and strengthen quality infrastructure.
- Design and implement targeted measures for SME internationalisation, including financial support mechanisms and trade insurance.
- Support SME cluster creation and integration into GVCs implementing the planned tax benefits for SMEs.
- Improve automated processes related to trade procedures, streamline border control, and reduce fees for smoother trade operations.
- Monitor and evaluate initiatives supporting SME access to global markets, attaching measurable targets to all promotion programmes.
- Align with EU legislation on accreditation and conformity assessment to eliminate trade barriers and enhance international co-operation.
- Continue to improve the market surveillance system.
- Create and implement an action plan for education about standardisation.

**Fostering innovation and business support**

- Develop a dedicated SME action plan with detailed costing for a stronger SME focus in the broader national economic policymaking.
- Facilitate access to external consultants who can provide specialised advice to SMEs.
- Consolidate initiatives for SME digitalisation through a single programme offering tailored assessment, roadmap, and financial support.
- Conduct a pilot project to rigorously evaluate the impact of select support programmes on SME performance.
- Expand innovation infrastructure by growing technology parks/incubators/:accelerators and realising the Absheron Valley cluster vision.
- Broaden financial incentives for innovation and R&D, targeting a wider range of SMEs beyond the IT sector.
- Incorporate an SME focus into targeted actions for green initiatives and aligned with environmental goals.
- Create implementation plans tailored to SMEs' size and capabilities to support green practices in a wide range of sectors.
- Increase focus on supporting green SMEs beyond the energy sector and leverage KOBIA's reach to promote resource-efficient practices.
- Enhance regulatory and financial incentives for greening practices among SMEs, to target businesses beyond the energy sector.
- Strengthen environmental monitoring tools that specifically address SMEs, facilitating a more accurate assessment of the impact of environmental policies on the SME sector.

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## Notes

[1] For more information on the analytical framework, please refer to the thematic chapter Digital Economy for SMEs

[2] Digital Azerbaijan is a digital information center covering portals that provide digital services in Azerbaijan, information on digital services and their use, information on events in this area, and surveys for civil thought for services. For more information, see https://www.digital.gov.az/digitalazerbaijan/en/page/about.

[3] The court must hold hearing and render its decision within one month of the date of receipt of the insolvency claim.

[4] *Suptech* stands for “supervisory technology”.

[5] *Twinning* is a European Union instrument for institutional co-operation between Public Administrations of EU Member States and of beneficiary or partner countries. See https://neighbourhood-enlargement.ec.europa.eu/funding-and-technical-assistance/twinning_en

[6] Through the platform available at www.kobim.az

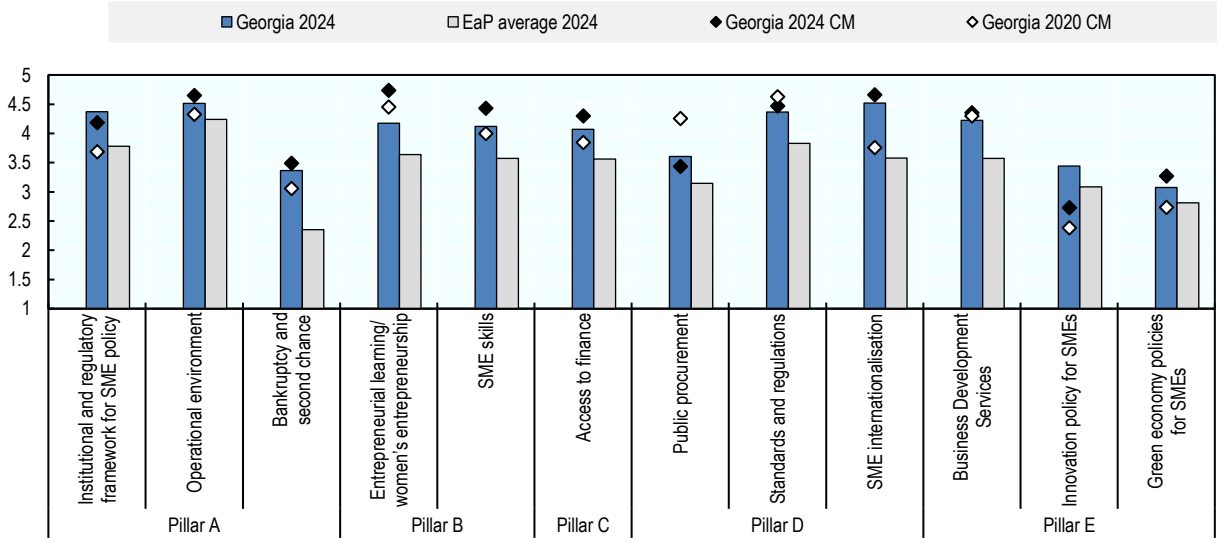
# 12 Georgia: Small Business Act country profile

This chapter provides an assessment of the progress made by Georgia in implementing the Small Business Act (SBA) for Europe over the period 2020-23. It starts with an overview of Georgia's economic context and dives further into the characteristics of the country's SME sector. It then develops on the state of selected framework conditions for the digital transformation of SMEs. Finally, it analyses Georgia's progress along twelve measurable dimensions grouped in five thematic pillars and sets out targeted policy recommendations.

## Key findings

### Figure 12.1. SME Policy Index scores for Georgia

Country scores by dimension, 2024 and 2020 vs 2024 CM




Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

StatLink https://stat.link/cw45y7

### Table 12.1. SME Policy Index scores for Georgia

Country scores by dimension, 2024 and 2020 vs 2024 CM

| Pillar | Dimension | Georgia 2024 | EaP average 2024 | *Georgia 2024 (CM)* | *Georgia 2020 (CM)* |
|---|---|---|---|---|---|
| Pillar A | Institutional and regulatory framework for SME policy | 4.37 | 3.78 | 4.19 | 3.69 |
| | Operational environment | 4.51 | 4.24 | 4.65 | 4.33 |
| | Bankruptcy and second chance | 3.36 | 2.35 | 3.49 | 3.06 |
| Pillar B | Entrepreneurial learning/ women's entrepreneurship | 4.17 | 3.64 | 4.74 | 4.45 |
| | SME skills | 4.12 | 3.57 | 4.43 | 4.00 |
| Pillar C | Access to finance | 4.07 | 3.56 | 4.30 | 3.85 |
| Pillar D | Public procurement | 3.61 | 3.15 | 3.44 | 4.26 |
| | Standards and regulations | 4.37 | 3.83 | 4.47 | 4.63 |
| | SME internationalisation | 4.52 | 3.58 | 4.66 | 3.76 |
| Pillar E | Business development services | 4.22 | 3.57 | 4.35 | 4.30 |
| | Innovation policy for SMEs | 3.44 | 3.09 | 2.73 | 2.38 |
| | Green economy policies for SMEs | 3.08 | 2.81 | 3.27 | 2.74 |

Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Table 12.2. Implementation progress on the SME Policy Index 2020 policy reforms – Georgia

| Priority reforms outlined in the SME Policy Index 2020 | Key reforms implemented to date |
|---|---|
| **Pillar A – Responsive Government** | |
| Elaborate a new SME Development Strategy beyond 2020.<br>Ensure that the RIA SME-test is systematically applied and results are taken into consideration in the legislative and regulatory approval process.<br>Streamline the insolvency framework by introducing out-of-court settlements and simplified insolvency proceedings for SMEs.<br>Introduce an early warning system for detecting insolvency.<br>Adopt a comprehensive second-chance strategy for bankrupt entrepreneurs. | Adoption of the SME Development Strategy for the period 2021-25.<br>Application of the Law of Georgia on Mediation in 2020 aiming to support alternative means of dispute resolution.<br>Adoption of the 2021 Law on Rehabilitation and Collective Satisfaction of Creditors, providing a new framework for insolvency.<br>Establishment in 2020 of the Digital Governance Agency and Digital Governance Strategy 2023-2026 due to be adopted. |
| **Pillar B – Entrepreneurial Human Capital** | |
| Address the European Entrepreneurship Competence Framework (EntreComp) across the curriculum and support it through pre- and in-service teacher training.<br>Consider an improved state-level intelligence framework for women's entrepreneurship.<br>Reinforce Georgia's Innovation and Technology Agency's (GITA's) online training developments to widen outreach to SMEs in outlying regions. | Development of a methodology for the organisational assessment of vocational schools, providing further efforts on harmonising entrepreneurial modules in vocational education and training (VET) programmes with EntreComp.<br>Creation of the Skills Agency, notably launching teacher networks to stimulate VET partnerships for teacher training.<br>Adoption of the SME Strategy for 2021-25 with a new priority direction dedicated to women's entrepreneurship.<br>Increase in online trainings for SMEs, provided by several stakeholders, including Enterprise Georgia, GITA, and the Georgian Chamber of Commerce and Industry (GCCI). |
| **Pillar C – Access to Finance** | |
| Support diversification of financing instruments to enable small businesses to access funding.<br>Complete the reform of the legal framework for leasing and factoring.<br>Further develop a framework for crowdfunding.<br>Continue efforts to reduce the level of dollarisation in the financial sector. | Publication of a Sustainable Finance taxonomy and related classification.<br>Introduction of a requirement on commercial banks to report monthly on green loans and publication of a climate-related Risk Radar.<br>Integration of ESG issues into the Corporate Governance Code for issues of Public Securities.<br>Relaunch and expansion of the national credit guarantee scheme due to the pandemic.<br>Adoption in 2023 of the Law on Microbanks, which creates a new 'Microbank' financial institution.<br>Amendments to the Law on Securities Market in spring 2022.<br>Adoption of a new National Strategy for Financial Education recognising SMEs as a target group.<br>Launch of the financial education website FinEdu in 2020. |
| **Pillar D – Access to Markets** | |
| Increase the scope of export readiness and SME-FDI linkages programmes provided by Enterprise Georgia and ensure they are evaluated.<br>Introduce financial support programmes for exporting SMEs.<br>Carry out evaluations of the legislation on technical regulations, metrology and market surveillance.<br>Improve the ability of contracting authorities to ensure greater competition. | Promotion of export growth and internationalisation of SMEs as priorities of the 2021-2025 SME Development Strategy.<br>Enterprise Georgia's 2022 Export Assistance Programme to co-finance technical assistance to exporting businesses.<br>Establishment of an independent Market Surveillance Agency.<br>Intensification of the approximation of national legislation with the EU *acquis*: the Georgian National Agency for Standards and Metrology's GEOSTM CEN and CENELEC Affiliate status in 2023.<br>Materials and trainings issued by the State Procurement Agency (SPA) for contracting authorities to facilitate SMEs' participation in public procurement. |
| **Pillar E – Innovation and Business Support** | |
| Develop a single information portal containing information on all institutions and agencies offering business support programmes.<br>Monitor the economic impact of the financial instruments introduced.<br>Strengthen linkages between businesses and research institutions/facilities.<br>Increase the role of demand-side policies to incentivise diffusion of innovations.<br>Create a single point of information for SMEs and an outreach body on green practices.<br>Incorporate policies to support SMEs greening into overall support for enhancing SMEs' competitiveness. | Enterprise Georgia's growth hubs increase awareness of support programmes and provide training and services to SMEs.<br>Creation of a department within Enterprise Georgia to monitor and analyse the impact of its SME support programmes.<br>GITA's technology transfer pilot programme to identify scientific outputs with commercial potential and assist research teams in negotiations with businesses.<br>Inclusion of the "Development of the Green Economy for SMEs" as a strategic direction in the SME Development Strategy 2021-2025. |

## Context

### *Economic snapshot*

Although Russia's war of aggression against Ukraine caused significant economic disruptions in 2022, the Georgian economy remained largely resilient and was negatively affected (in the short-term only) by supply chain disruptions, commodity price hikes and exchange-rate volatility. GDP growth for 2022 reached 10.1%, building on a strong post-COVID recovery with double-digit growth of 10.5% in 2021 driven by the gradual lifting of restrictions and expansion in the services, industry and agriculture sectors (World Bank, 2023[1]). Georgia capitalised on the large number of highly skilled individuals coming into the country, fuelling domestic consumption, and it benefitted from the relocation of businesses from Russia, as well as increasing transport flows. In the period January-November 2022, migrants accounted for 32% of rental demand and 5.5% of apartment sales in Tbilisi (TBC Capital, 2022[2]).

Despite the positive trend, Georgia has suffered from high inflation since 2021. Annual inflation remained in the double digits throughout 2022, though in December 2022 it fell to 9.8% and in June 2023 to 0.6% thanks to appropriate monetary and fiscal policy measures (Geostat, 2023[3]). The pandemic significantly affected both exports and imports in 2020, with a year-on-year change of -17.5 and -7.2 percentage points as a share of GDP, respectively (World Bank, 2023[4]). However, in 2021 trade showed signs of recovery and the strong growth continued in 2022, with Georgia's foreign trade turnover going up 33.4%, driven by exports of copper ores and concentrates, cars, ferroalloys, fertilisers, wine, and spirits (Geostat, 2022[5]).

### Table 12.3. Georgia: Main macroeconomic indicators, 2018-22

| Indicator | Unit of measurement | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|
| GDP growth** | Percent, year-on-year | 4.8 | 5 | -6.8 | 10.5 | 10.1 |
| Inflation** | Annual percent increase, consumer prices | 2.6 | 4.9 | 5.2 | 9.6 | 11.9 |
| Government balance[1] | Percentage of GDP | -2.3 | -2.1 | -9.3 | -6.1 | -3.1 |
| Current account balance* | Percentage of GDP | -6.8 | -5.9 | -12.5 | -10.4 | -4.1*** |
| Exports of goods and services* | Percentage of GDP | 50.6 | 54.8 | 37.3 | 43.2 | 52.9 |
| Imports of goods and services* | Percentage of GDP | 61.2 | 63.8 | 56.6 | 59.6 | 63.0 |
| FDI net inflows*** | Percentage of GDP | 7.7 | 7.7 | 3.7 | 6.7 | 8.1 |
| General government gross debt** | Percentage of GDP | 38.9 | 40.4 | 60.2 | 49.7 | 39.8 |
| Domestic credit to private sector* | Percentage of GDP | 60.5 | 65.6 | 79.9 | 73.8 | 64 |
| Unemployment[2]* | Percentage of total active population | 19.2 | 17.6 | 18.5 | 20.6 | 17.3 |
| Nominal GDP** | USD billion | 17.6 | 17.5 | 15.8 | 18.6 | 24.6 |

[1] General government augmented net lending/borrowing, agreed with IMF-Ministry of Finance.
[2] Modelled International Labour Organisation estimates.
Note: GDP: gross domestic product.
Sources: * (World Bank, 2023[6]); ** (IMF, 2023[7]); *** GEOSTAT/National Bank of Georgia.

The ICT sector has become increasingly important to Georgia's economy, accounting for 4.7% of GDP and posting 49.9% year-on-year growth rate in 2022 (PMCG, 2023[8]). Mirroring global trends, Georgian businesses started adopting digital solutions in their operations during the pandemic, with 42% of firms having started or increased online business activity by October 2021 (World Bank, 2021[9]). More specifically, 40% of small, 43% of medium and 35% of large enterprises did so (World Bank, 2021[10]). In 2020, e-commerce sales increased threefold, although their share in total retail trade remained at 6.5% as of 2021. As of 2022, 17% of Georgian enterprises used digital solutions, such as cloud infrastructure, process management systems (e.g. ERP). Large companies have the highest adoption rate, at 35%, medium-sized enterprises at 26% and small companies at 16%. The Business Demand on Skills Survey also shows that the larger the company, the greater the incentive to invest in technology, with 19% of large firms indicating such intentions compared to only 3% of small firms (MoESD, 2022[11]).

### Box 12.1. Georgia's support for SMEs during the COVID-19 pandemic

During the COVID-19 pandemic, the Georgian government introduced several crisis alleviation strategies, providing several options for SMEs to access finance through Enterprise Georgia.

**Financial support**

Co-financing and credit guarantee programmes included:

- Interest rate co-financing increase from 7% to 11.5% (credit) and from 9% to 13.5% (leasing); the maximum duration of co-financing was extended to 36 months.
- The broadening of the sectoral scope of the credit guarantee mechanism, increased guarantee amounts from 70% to 90% on new loans and 30% on restructured loans.
- The Business Universal Programme allowed beneficiaries of the credit guarantee scheme to also receive an interest rate subsidy and grant.
- Micro Grants program allowed for increased amounts (from GEL 20 000 to 30 000), decreasing co-financing rate from 20% to 10%, with an additional 5% co-financing rate for beneficiaries from mountainous regions.
- A sector-specific programme for hospitality and construction industries offered a co-payment of accrued interest rate on the existing loans of micro and small-sized hotels and introduced a mortgage loan subsidy scheme.
- A mechanism of subsidising bank guarantees allowed financing a guarantor's guarantee fees for six months, used to cover the beneficiary's liabilities.

**Regulatory flexibility**

In 2020-21, the Georgian government introduced temporary measures in terms of its tax policy:

- An income tax exemption for individuals with a monthly income not exceeding GEL 1 500 (EUR ~530), with the exemption applied to GEL 750 (EUR ~260) out of GEL 1 500 (EUR ~520).
- A property tax exemption for businesses in tourism and postponed income tax.
- The fully automated VAT refund system was launched to support economic activity.

**Workforce support**

Targeted support measures were launched for female employees and entrepreneurs (198 000 beneficiaries) and minimal compensation offered to self-employed individuals who lost their incomes.

**Market support**

The "Business Support" Programme offered co-financing of interest rates on loans and leases (between GEL 10 000 and GEL 10 million (EUR ~3 500 and EUR ~3.5 million); a credit guarantee maximum of 60% of the approved loan for up to 10 years; and a grant covering up to 15% of the approved loan. In 2022, the programme was expanded to include technical assistance to exporter companies, in areas such as product licensing and certification, branding, and stimulation of international sales.

**Measures to improve access to digital infrastructures**

Vocational education and training (VET) institutions were supported by creating distance learning modules and a unified e-database for teachers and programme managers, including by holding information sessions and workshops.

Source: (Enterprise Georgia, 2023[12]).

Even though Georgia has achieved a significant level of macroeconomic stability, further reforms are needed to ensure inclusive growth and competitiveness in the long run. Key priorities include education reform to strengthen human capital and ensure skills for the labour market and innovativeness, as well as strengthening physical infrastructure including transport and green energy infrastructure to facilitate access to global value chains (European Commission, 2022[13]).

### *SME sector*

Georgia's National Statistics Office has not changed its approach to classifying businesses according to their size since 2017. Georgia's SME thresholds differ from EU criteria, as microenterprises are placed under the small enterprise category (Table 12.4).

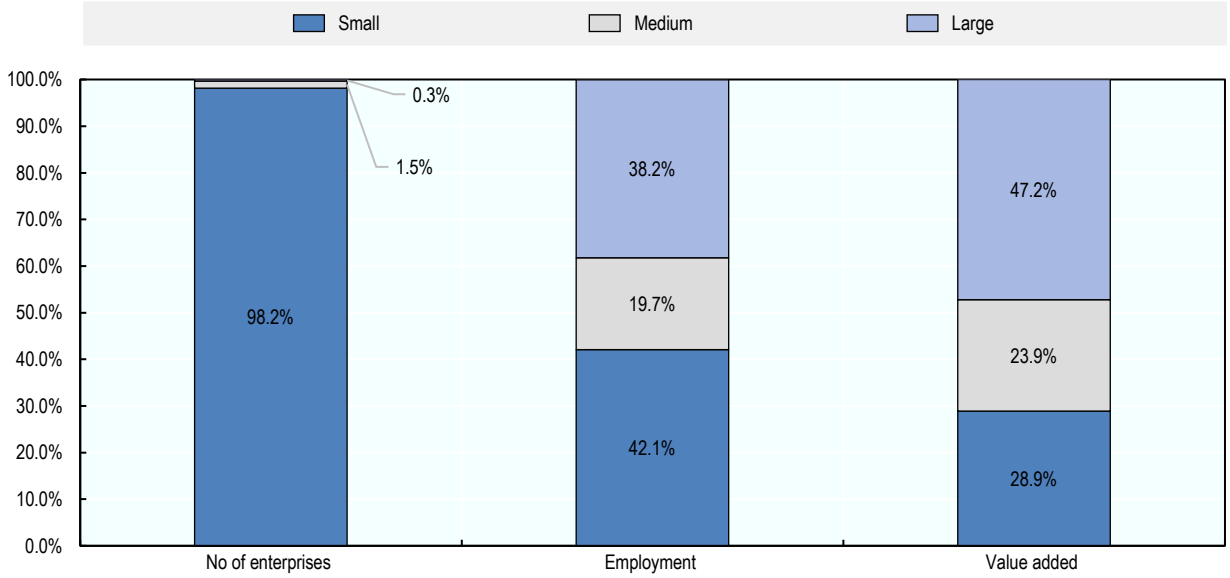
**Table 12.4. The SME definition in Georgia**

| | Small | Medium |
|---|---|---|
| Employment | ≤ 50 employees | ≤ 250 employees |
| Turnover | ≤ GEL 12 million (EUR ~4 217 880) | ≤ GEL 60 million (EUR ~21 089 400) |

Note: Exchange rate as of 28 September 2023 (OANDA, n.d.[14]).
Source: (Geostat, 2023[15]).

SMEs constitute a large segment of the business sector, making a significant contribution to the turnover, value added and employment. In 2021, small businesses represented 98.2% and medium-sized enterprises 1.5% of the total business sector. While the number of employees in SMEs has been increasing since 2015, there was a significant drop in employment in 2020 (-10.1%) due to the pandemic and, despite the post-pandemic recovery in 2021, employment in SMEs is still lower than pre-pandemic levels. In 2021, SMEs employed 61.8% of the workforce in the business sector (Figure 12.2). In terms of turnover and value added, SMEs experienced an upward trend in the 2015-21 period, except in 2020 when turnover declined by 1.8 percentage points and value added by 2 percentage points. SMEs' share in the total business sector value added varied between 53% and 61% during the observed time frame, with the lowest share, 53%, in 2021.

## Figure 12.2. Business demography indicators in Georgia, by company size (2021)



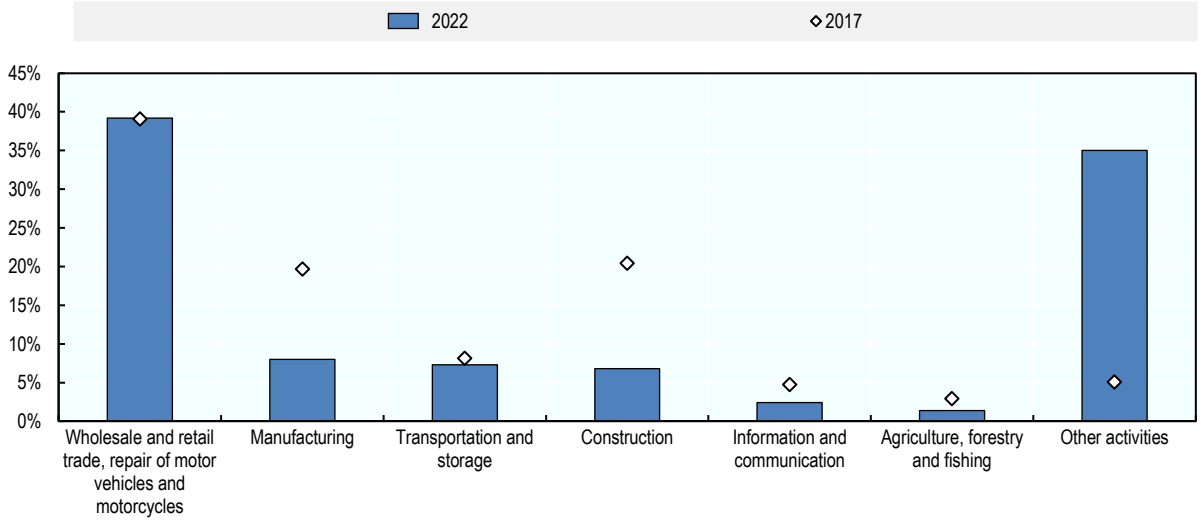

Source: (Geostat, 2022[16]).

StatLink https://stat.link/0cyknx

Looking at the sectoral distribution, most SMEs in Georgia are concentrated in low value-added sectors, such as wholesale and retail trade (39.4%), followed by transport and storage (7.5%) and construction (7%) (Figure 1.3). While the share of SMEs in wholesale and retail trade remained nearly stable in the period between 2017 and 2022, the share of construction and manufacturing decreased substantially, by almost 14 and 12 percentage points respectively.

## Figure 12.3. Sectoral distribution of SMEs in Georgia (2022)

Share of SMEs by type of economic activity




Note: "Other activities" includes NACE Rev. 2 sectors B, D, E, I, K to U, and activity unknown.
Source: (OECD, 2020[17]); (Geostat, 2023[15]).

StatLink https://stat.link/1uhz3w

## SBA assessment by pillar

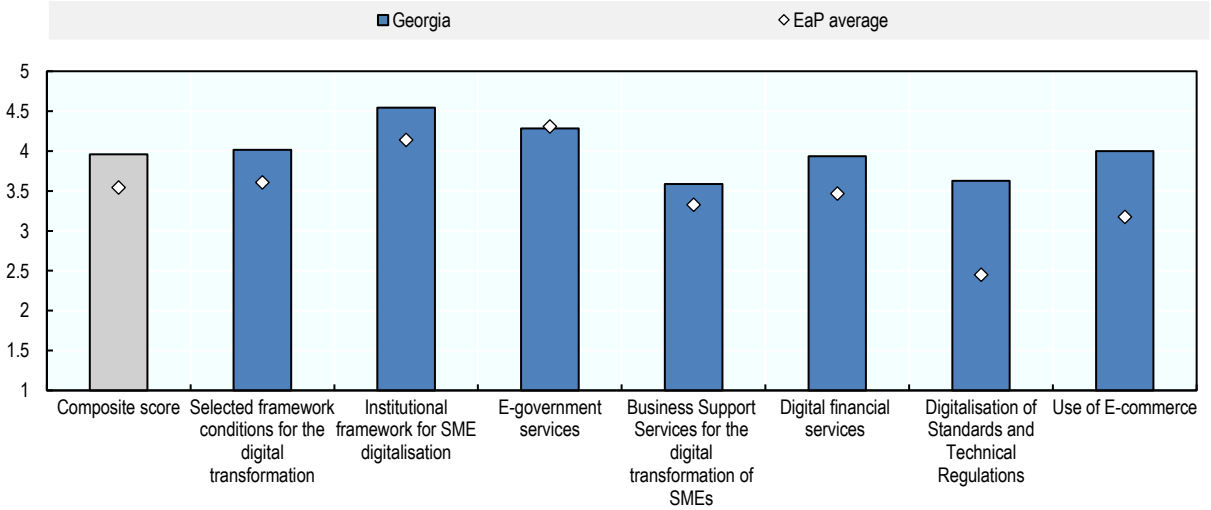
### *SME digitalisation policies*

Creating an environment conducive to the digital transformation of SMEs requires a comprehensive policy approach based on sound framework conditions for the digital economy as well as targeted support to help SMEs reap the benefits of digital solutions. Framework conditions refer to pre-requisites for the digital transformation, such as affordable access to high-speed broadband, a satisfactory level of digital literacy among citizens, and a well-co-ordinated and coherent policy approach and governance system for digital policies. In the context of SME development, those fundamentals need to be complemented with specific business support services, digital financial services for SMEs, and tailored support to engage in e-commerce to reach new markets.

Reflecting the multi-faceted nature of the topic, this round of SBA assessment evaluates EaP countries' policy approaches to SME digitalisation through i) a dedicated pillar on selected framework conditions for the digital transformation, as well as ii) six new sub-dimensions, incorporated in the pre-existing dimensions of the SBA assessment, to delve deeper into specific thematic policies to foster the digital transformation of SMEs. The weighted average of the scores for the new pillar and digitalisation-oriented sub-dimensions results in a composite score for SME digitalisation policies presented below (Figure 12.4).[1]

Georgia appears as top performer in SME digitalisation policies, with a composite score reaching 3.96. The country scores above 4 for four of the seven aspects evaluated, and almost systematically above the regional average, apart from e-government services. This performance reflects Georgia's overall substantial efforts to accelerate the digital transformation, with the development of a strong institutional and policy framework and dedicated initiatives. Support services for SME digitalisation have notably been recently launched in the new Growth Hubs. Moving forward, this could be complemented by additional measures such as digital skills development programmes directed specifically to managers of SMEs and the establishment of a network of certified consultants that can provide advisory services on business digitalisation in your country. Strong co-ordination should also be continuously ensured between Enterprise Georgia and GITA on these topics.

### Figure 12.4. Scores for SME digitalisation policies in Georgia




Note: Further details on the assessment and calculation methodology can be found in the "Assessment framework" section in the Digital Economy for SMEs chapter, in the "Policy framework, structure of the report and assessment process" chapter and in Annex A. Additional information on institutional framework for SME digitalisation and e-government services can be found in Pillar A; on digital financial services in Pillar C; on use of e-commerce in Pillar D; and on Business support services for the digital transformation of SMEs in Pillar E.

StatLink https://stat.link/4ltgck

The following section details Georgia's performance in developing selected framework conditions for the digital transformation, while more information on digitalisation-oriented sub-dimensions can be found in the sections on the pillars they respectively belong to.

### *Selected framework conditions for the digital transformation*

Individuals and firms, notably SMEs, cannot fully reap the benefits offered by the digital transformation without the existence of robust framework conditions, such as comprehensive digitalisation policies, access to high-speed Internet and well-rounded ICT skills among the population. Accessible, affordable and stable broadband connection is indeed the *sine qua non* to ensure widespread participation of citizens and businesses in the digital economy, and to stem the widening of the connectivity gaps between urban and rural territories, and between firms of different sizes. Furthermore, fostering digital skills development at all stages of life through formal education and lifelong learning initiatives for adults is essential to help the working-age population acquire the skills they need to embark on the digital transformation, produce tech-savvy consumers, and build a talent pool of IT specialists.

#### *National digital strategy*

Georgia does not yet have a comprehensive national digital development strategy as a standalone document. The Ministry of Economy and Sustainable Development (MoESD), with the technical assistance of the World Bank, has developed a draft strategy (*Long-term National Strategy for the Development of the Digital Economy and Information Society*) and an implementation plan, but the document has not yet been adopted. The latest update suggests that the document has been proposed to the government and approval is pending. According to the government, the strategy will act as an umbrella document and cover several digital economy objectives: digitalisation of the public and private sectors, increasing digital literacy, facilitating the formation of an information society, boosting high-tech exports, developing research and innovation, and increasing Georgia's competitiveness in the global digital economy.

So far, digital economy objectives and strategic actions have been integrated into several policy documents. First, Georgia's primary long-term strategic document – Vision 2030 – establishes the digital economy and information technologies as one of the 13 key aspects of the country's economic development. The strategy envisions positioning Georgia as a globally integrated "digital hub". Several priority directions are defined to achieve this goal: providing high-speed Internet access to businesses and government institutions; increasing competitiveness in the broadband market; attracting investments; developing skills; and enhancing digital literacy, generating demand, developing e-commerce platforms, boosting high-tech exports, etc. The strategy also envisions increasing digital economy access for people with disabilities. Moreover, advancing cybersecurity is a critical aspect of the information society, with a key role in the development of the digital economy.

In addition, the *National Broadband Development Strategy of Georgia* (NBDS) and its Action Plan for 2020-2025 aim at maximising broadband coverage. Digitalisation is also included in the *SME Development Strategy of Georgia 2021-2025*, which notably seeks to increase SMEs' access to information technologies, develop digital skills among entrepreneurs, develop broadband infrastructure and promote e-commerce. Finally, several policy documents envision the digitalisation of the public sector, including the *Public Service Development Strategy of Georgia 2022-2025* and the Georgia Revenue Service's *Services Development Strategy 2021-2024*. The *Public Service Development Strategy of Georgia 2022-2025* establishes "mostly digital" as a core principle for the development and provision of government services. Moreover, the *Digital Governance Strategy 2023-2026* has been developed and will soon be adopted. In this regard, Georgia has already made progress in recent years, with the share of individuals using the Internet to interact with public authorities steadily increasing – from 11.8% in 2018 to 17% in 2021.

In terms of institutional framework, Georgia has worked on developing a multi-stakeholder approach. The draft *Long-term National Strategy for the Development of Digital Economy and Information Society* and its

implementation plan were developed by a multi-stakeholder working group, which included private sector representatives, notably business associations, NGOs and World Bank experts. The MoESD has a clear mandate to lead digitalisation policies through its Communications, Information and Modern Technologies Department. With regard to the implementation of existing policy documents, further efforts have been made to foster co-ordination among stakeholders: the NBDS, for instance, is co-ordinated by a dedicated high-level steering committee made up of deputy ministers and heads of state agencies.

However, the co-existence of several policy documents covering digitalisation increases the risk of overlap. The upcoming National Digital Strategy would be a good opportunity to ensure policy coherence and offer an overarching vision. Moreover, while Georgia's IT sector has been booming, the existing policy documents entail fewer measures for the digitalisation of SMEs in non-IT sectors – a few initiatives have been implemented and the topic is mentioned in the SME strategy, but the measures so far have been mostly limited to digital skills development. Enterprise Georgia is, however, working on developing a new, comprehensive support programme.

Moving forward, Georgia should adopt its National Digital Strategy, ensuring its comprehensiveness and setting clear objectives, actions, resources and task allocation. Thereafter, it should ensure suitable measures for monitoring and evaluating the strategy. It should also grant greater consideration to the digital transformation of firms in non-IT sectors in policy documents and related initiatives, and encourage the development and uptake of more advanced technologies such as artificial intelligence, big data analytics and blockchain – to further advance on Georgia's ambition to become a "digital hub".

### *Broadband connectivity*

The development of a high-speed access appears as a priority in the government's agenda. In 2020, the country adopted its first national broadband strategy – the above-mentioned NBDS and its Action Plan for 2020-2025, which is in line with the EU's Gigabit Society Objectives 2025. The NBDS was developed by the MoESD with technical assistance from the European Commission, the World Bank and EU4Digital. The strategy has three key policy objectives: 1) increasing competition; 2) attracting investments; and 3) building digital skills and demand.

Monitored by the dedicated high-level co-ordination group mentioned above, the implementation of the strategy is further fostered by annual multi-stakeholder consultations and various meetings, including with local municipalities and telecom operators. The MoESD and the Communications Commission (ComCom) organise such meetings to get feedback about the programme implementation. The results of these evaluations are discussed and reflected in the strategy. Moreover, Georgia collects indicators to track progress, many of which are publicly available on ComCom's website (comcom.ge).

Data reveal that Georgia's policy efforts have already borne fruit: the country is one of the most connected EaP countries, registering an increase of about 50% in both fixed and mobile broadband subscriptions between 2015 and 2020. Moreover, the digital divide between urban and rural areas more than halved over that period (-64%), down to 12.6% in 2021. This figure remains considerable, ranking above the regional average and EU values – but additional measures are planned to tackle the remaining gap. The NBDS has a target to eliminate the remaining divide and cover 99% of the Georgian territory with 4G by 2025. This objective is also mirrored in the mission of the Open Net – a government programme in charge of the project Log-In Georgia, which foresees the development of the high-quality broadband infrastructure in Georgia's regions. Other measurable targets set under the NBDS for 2025 include: pilots for 5G services in three municipalities; all institutional entities having access to 1 Gbps connectivity; and all households and enterprises having access to high-speed (100 Mbps+) broadband networks.

However, subscriptions for both fixed and mobile broadband remain below OECD and EU levels. This might be partly due to persisting challenges in terms of affordability: prices for fixed broadband have come down in recent years, but remain slightly above the ITU's 2% target, amounting to 2.35% of gross national income (GNI) per capita in 2022. Internet speed in firms could be further improved, as the majority of

connected firms have an average Internet speed below 30 Mbit/s (61% in 2023). This poses a particular problem for SMEs, who lag behind broadband uptake compared to large firms: 79% of large firms benefit from high-speed Internet (above 30 Mbit/s), while only 54% of medium ones and 38% of small ones do. Further targeted actions are therefore needed to close this substantial gap.

Moving forward, Georgia could foster competition, investment, and innovation to ultimately support faster Internet at lower prices; strengthen the demand side by ensuring consumers' access to information on broadband services and quality; and promote SMEs' uptake of high-speed Internet.

### *Digital skills*

The development of digital skills is a key aspect of several policy documents integrating digital economy objectives. The NBDS, for instance, establishes building digital demand and skills as one of its three priority areas. In accordance with this objective, the action plan defines relevant actions in several directions: support of digital skills/digital literacy development programmes and state campaigns, including awareness-raising about cybersecurity; promotion of broadband service utilisation across socially vulnerable households; targeted programmes to ensure adapted Internet content is available for people with disabilities. Additional policy efforts are being provided to foster digital skills development among businesses, with the SME Strategy 2021-2025 entailing two objectives to this end. The topic should also be covered by the upcoming National Digital Strategy.

So far, ICT skills have been given increasing importance in vocational education and training (VET)education. Embedded in the VET development strategies 2013-2020 and draft for 2023-27, they already constitute a mandatory competence to acquire in VET curricula and should be further fostered by efforts to establish co-operation between educational organisations and businesses: the ICT cluster, together with its member companies, is developing a model that will support educational organisations to come up with practical approaches tailored to the current needs of the private sector.

Beyond education systems, Georgia has successfully implemented several lifelong learning initiatives, provided by both the public and private sectors, to promote ICT skills development among the general population. Georgia's Innovation and Technology Agency (GITA) is one of the main stakeholders in that regard, offering a number of free online trainings and certifications on its dedicated platform ict.gov.ge. GITA also led a *Digital Economy Skills Development Programme* to train and certify 3 000 Georgian citizens in the most demanded digital skills by March 2023. Many of these opportunities benefit from donor support, such as the *Industry-led Skills Development Programme*, led by the US Agency for International Development (USAID), and the World Bank-financed *Log-in Georgia Project* (2020-2025). The latter encompasses a Digital Adoption Programme, implemented by the National Communication Commission, to equip citizens with basic digital skills, notably in rural areas through training seminars based on the Community Needs Assessment. It has already been launched in four municipalities and has so far resulted in the conduction of 180 training seminars on digital literacy and safe use of the Internet. Additional activities are being carried out regarding e-government services, e-Auction and online consumer protection. The Programme has benefitted over 2,000 individuals so far.

Moreover, Georgia regularly collects data on ICT skills levels at the national level and among university and VET graduates, which facilitates monitoring and evaluation of policy measures. Students' progress in acquiring digital competences is reportedly assessed.

However, digital skills levels in Georgia remain below OECD and EU values, with 36% of Georgians having only basic digital skills in 2021 (a share similar to that of Ukrainians). Moreover, efforts on digital literacy in education systems have been focused on VET so far, with digital competence being included only in VET curricula. Despite the number of educational programmes and initiatives available, the country does not yet have a framework for certification comparable to the EU E-Competence Framework. As the dissemination of ICT skills advances in the population, the absence of such a framework can potentially lead to inconsistencies in digital skills assessment, difficulties in recognising digital competences and

limitations for career development. Finally, in terms of monitoring and evaluation, key performance indicators assessing digital skills policies could be improved to better capture impact.

Moving forward, Georgia could implement digital competence as a key competence at all levels of education, also providing for relevant teacher training; introduce a digital competence framework to establish a standardised set of criteria and standards for assessing, certifying and recognising digital competences; complement existing skills assessment and anticipation tools with aspects on digital skills; and complete the adoption and implementation of a National Digital Skills and Jobs Coalition to foster the inclusion of all relevant stakeholders, including education providers and teachers, in the design and implementation of digital skills policies.

## *Pillar A: Responsive government*

### *Institutional and regulatory framework*

Georgia has continued strengthening its already advanced institutional framework and made further progress in aligning its practices to EU standards. With the launch of a new SME Strategy 2021-2025, the priority scope has been broadened to include the development of entrepreneurial skills, green economy and SME digitalisation support.

#### Institutional setting

According to the 2020 EaP SME Policy Index, Georgia had already established a well-structured and advanced institutional and regulatory framework for SME policy. Since the previous SBA assessment, Georgia has approved and is currently implementing its second multi-year SME Development Strategy for 2021-2025 and related Action Plans for 2021-2022 and 2023-2025. The strategy was built upon the achievements and progress made by the previous SME Development Strategy for 2016-2020, which was implemented successfully, with all defined targets having been achieved.

The new strategy for 2021-2025 was elaborated in the same inclusive manner as the previous one. A Steering Committee and a Working Group were established to involve representatives of state institutions, civil society and business associations. The document was elaborated in co-operation with the OECD and GIZ, with the support of the EU.

The new strategy is articulated along seven strategic directions: i) refining legislation, institutional strengthening and improving of the operational environment for SMEs; ii) promoting the development of entrepreneurial skills and raising the entrepreneurial culture of SMEs; iii) improving access to finance for SMEs; iv) promoting the export growth, access to the market, and internationalisation of SMEs; v) promoting electronic communications, information technologies, innovation, and research and development for SMEs; vi) promoting the development of women entrepreneurship; and vii) promoting the development of a green economy for SMEs. It involves 42 objectives and 84 corresponding outcome indicators. The document identifies three quantitative targets at the aggregate level related to SME growth, employment generation and increasing productivity.

Like the previous strategy, the new SME Development Strategy 2021-2025 includes an evaluation and monitoring system. To determine the progress of the activities defined by the accompanying action plans, the Economic Policy Department of the MoESD regularly monitors implementation. The annual reports on the implementation of the strategy and corresponding action plans are published on the ministry's website. Currently, implementation is advancing as planned, despite the disruptions caused by the COVID-19 epidemic and economic shocks created by the war in Ukraine.

The MoESD, along with two key public agencies – Enterprise Georgia and GITA – is in charge of SME policy implementation. Both agencies were established in 2014. Enterprise Georgia has substantial

operational autonomy and is in charge of overall SME support services. GITA leads the innovation and technological development component of the strategy.

Since 2020, Georgia has made progress in updating and completing the legal framework for SME policy. In 2021, the parliament adopted the new Law on Entrepreneurs, which entered into force in 2022. The new law aims to fulfil the requirements of the association agreement and association agenda and the approximation of Georgia's corporate law to EU legislation. The Law of Georgia on Mediation entered into force on 1 January 2020. It aims to support alternative means of dispute resolution to develop the legislative framework related to mediation. In addition, the Law of Georgia on Rehabilitation and Collective Satisfaction of Creditors, adopted in 2020, has been enacted since April 2021. By adopting this mentioned law, a progressive framework governing the insolvency process was established in Georgia, incentivising the rehabilitation of enterprises (see below).

#### Legislative simplification and RIA

Georgia has also made significant progress towards the systematic application of regulatory impact assessments (RIA), even though the use of the RIA mechanism is not fully institutionalised. In addition to the unit in charge of RIA within the MoESD, established in 2007, the Parliamentary Secretary of the Government Administration of Georgia was assigned the mandate of RIA quality control. In line with the obligation to perform RIA for legal amendments initiated by the government concerning 20 typologies of laws defined by the Organic Law of Georgia on Normative Acts, the government of Georgia has adopted the RIA methodology, defining the technical guidelines for implementing RIA evaluations and elaborating the relevant reports. However, despite important steps made so far, there are still concerns about public agencies' lack of willingness and capacity to provide quality RIA reports and incorporate the mechanism into their daily policy making.

Although RIA is formally mandatory, the methodology provides the possibility of avoiding it for significant legal initiatives by setting a list of exceptions and excluding legal acts initiated by members of parliament. The methodology for SME-specific RIA tests has still not been adopted and is currently under development.

#### Public-private consultations

Public-private consultations (PPCs) are regularly conducted, and public-private institutions, including the Business Ombudsman, the Investors Council and the Private Sector Development Advisory Council, are actively engaged in promoting public-private dialogue. In 2022, the government approved the Instruction on Public Consultations, which is Annex N11 of the Ordinance of the Government "On Rules for Policy Elaboration, Monitoring, and Evaluation". According to this instruction, consultations are a crucial procedure and need to consider the extensive involvement of all stakeholders not only for the purpose of being informed on planned changes/reform but also to be actively engaged in elaborating policy priorities and completing the development of the policy cycle.

#### Institutional framework for SME digitalisation

The SME Development Strategy 2016-2020 and the SME Development Strategy 2021-2025, and related action plans, cover a complex range of issues. In terms of SME digitalisation, most attention has been focused on fostering digital innovation through relevant objectives and targeted activities. "Promotion of Electronic Communications, Information Technologies, Innovations and Research and Development for SMEs" is one of the priority directions of the Strategy 2021-2025, with a view to increasing the competitiveness and productivity of SMEs. The objectives set in the Strategy include: innovative financing, in order to increase the productivity and innovation capacities of SMEs, as well as to increase the level of innovation in the country; supporting the development of e-commerce in SMEs through consulting and training activities; and fostering access to high-speed Internet for SMEs.

In order to step up support for the digital transformation of SMEs in non-IT sectors, which had received limited attention before, Enterprise Georgia has provided efforts to this end through a project conducted under the Georgia Relief and Recovery for Micro, Small, and Medium Enterprises project: Regional Consulting Centers (Growth Hubs). To achieve the goals of the project, Enterprise Georgia has centrally hired Digital Transformation Experts, who create tailored and detailed digital transformation plans for SMEs. The plans include recommendations for trainings on the specific digital skills needed, as well as which digital tools need to be acquired to improve internal processes. SMEs may benefit from a co-financed grant of up to 25 000 GEL (EUR ~8 800).

#### The way forward

To further improve the institutional and regulatory framework for SMEs, Georgia should guarantee a high-level of co-ordination between Enterprise Georgia and GITA to ensure that programmes supporting SME digitalisation and ICT sector development are developed in synergy. In addition, Georgia should consider the elaboration of specialised development strategies for sectors such as tourism, hospitality, or ICT, which inherently require a co-ordinated approach and the development of a supportive eco-system to thrive effectively.

### *Operational environment for SMEs*

Georgia has achieved notable global recognition for establishing a high-standard regulatory and business environment through a consistent and ongoing reform process and the establishment of several robust and autonomous institutions. Over the past year, the focus has shifted towards the provision of a wide set of government services via digital platforms, simultaneously improving accessibility, transparency, speed of delivery and cost efficiency.

#### E-government services

The implementation of the e-Georgia strategy (2014-2018) and its related action plans led to a number of achievements with regards to the development of advanced government platforms. The platforms my.gov.ge and data.gov.ge were already recognised in the previous EaP SME Policy Index assessment. my.gov.ge incorporates up to 730 e-government services, including business registration, reorganisation and bankruptcy registration, while data.gov.ge is an open data portal integrating public information on government activities or the decentralised system of public halls offering a number of services to citizens and organisations.

It should be noted that the e-Georgia 2014-2018 strategy dedicated to digital governance has not been updated. However, since the previous assessment, the Public Administration Reform (PAR) Strategy for 2023-2026 and related Action Plan for 2023-2024 have been adopted, covering the aspects of digital governance relevant to SMEs. Moreover, the Public Service Development Strategy 2022-2025 and related Action Plan 2022-2023 were also adopted in 2021. The strategy is based on several fundamental principles, including transparency, flexibility (timeliness and adaptability), mostly digital, etc. In addition, the accessibility of information technologies is one of the objectives within one of the priority directions of the SME Development Strategy of Georgia for 2021-2025.

In 2020, the Digital Governance Agency was established following the merger of two agencies under the Ministry of Justice – Smart Logic and the Data Exchange Agency. The agency is committed to providing safe, efficient, “one-stop” delivery of state electronic services to citizens, businesses and the non-governmental sector; to operating the unified government services portal my.gov.ge; and to achieving a form of governance based on the digital trust principle. The Digital Governance Strategy 2023-2026 is due to be adopted in 2023; a draft is already available.

#### Company registration

Georgia has one of the easiest company registration processes in the world. Company registration procedures have been further optimised since the previous assessment. They can be fully conducted online, require a single operation and are completed in one day.

#### Business licensing

Georgia's regulatory reform policy is characterised by a substantial reduction in the number of business licenses, as noted in the previous assessment. In addition, the system of licenses and permits is also based on the "silence implies consent" principle. Most remaining licenses are requested and granted through the electronic portal eauction.ge. Electronic management of licenses enhances flexibility, efficiency and the transparency of procedures. Several changes have been implemented over the past four years to further simplify the license administration process.

#### Tax compliance procedures for SMEs

Georgia has introduced a preferential taxation regime for micro and small enterprises. Microenterprises with an annual turnover under GEL 30 000 (EUR ~10 500) are exempt from income tax. Enterprises with an annual turnover less than GEL 500 000 (EUR ~175 000) have the possibility to acquire a small business status and pay turnover tax at a rate of 1% instead of 20% of net income/profit. Since the corporate income tax reform in 2017, all firms operating in Georgia's non-financial sector pay 15% only on distributed profit and are subject to a dividend tax of 5%. The corporate income tax (CIT) on retained/reinvested profits has been abolished. Extension of this CIT model to the insurance sector is planned from January 2024. As for the value-added tax (VAT), the threshold is set at GEL 100 000 (EUR ~35 000). Importantly, the government of Georgia has introduced an automatic VAT refund system which positively affected the financial standing of Georgian enterprises. The introduction of automatic refunds is one of the key steps to improve tax administration. Notably, good practices for VAT refund claims were established in 2019, but automatic payment became operational in the following years. The most recent tax reforms also relate to the simplification of tax administration. The Revenue Service of Georgia recently launched the Informational and Methodological Hub[2] to ease the burden of tax compliance in general and for enterprises in particular. This is expected to reduce tax disputes by making tax administration more predictable.

In addition, the Ministry of Finance is considering the implementation of the tax dispute resolution reform to improve the efficiency of tax dispute resolution by developing a new system and a fully dedicated, qualified and independent tax dispute resolution government body. Furthermore, the Revenue Service is currently working with the World Bank to improve SMEs' tax compliance using insights from behavioural economics.

#### The way forward

In order to continue improving the operational environment for SMEs, Georgia should i) complete the approval of the Digital Governance Strategy 2023-2026; ii) increase co-ordination among the different agencies and branches of the public administration, in order to achieve a high level of inter-operability among public sector data banks and to facilitate the exchange of data within the public administration; iii) increase cybersecurity in order to reduce the risks of hacking and sabotage; and iv) systematically calculate the effective tax rate imposed on different types of SMEs and review the impact of preferential tax regimes on enterprise growth.

### *Bankruptcy and second chance*

The adoption of the new "Law on Rehabilitation and the Collective Satisfaction of Creditors' Claims" in September 2020 significantly transformed and improved the Georgian insolvency regime. The newly

enacted legislation, effective since April 2021 and developed in high compliance with international standards, superseded the previous Insolvency Law adopted in 2007. This updated legal framework brought a noteworthy shift of focus from liquidation to rehabilitation, thereby efficiently addressing one of the main shortcomings of the previous regulatory regime. The new law introduced different mechanisms that incentivise the initiation of preventive reorganisation procedures at early stages of financial distress, including an out-of-court proceeding (the Regulated Agreement). Moreover, under the new regime, a moratorium on creditors' claims is automatically applied when an insolvency case proceeding is initiated, and tax debts no longer take the highest priority during bankruptcy proceedings. In addition, the law sets provisions to establish an electronic case management system for official information and documentation. However, the system is yet to be developed. Finally, the newly established insolvency practitioners are regulated by the National Bureau of Enforcement, which operates under the direction of the Ministry of Justice (EBRD, 2021[18]).

The insolvency reform is monitored and evaluated under the project ReforMeter, a reform-tracking tool supported by the USAID Economic Governance Programme and implemented by ISET Policy Institute.[3]According to a preliminary assessment of the reform carried out in this context, while under the previous law the share of cases that started under the rehabilitation regime as opposed to the bankruptcy regime represented only 10% of all cases, under the new law the share increased to 35%. Moreover, the new reform is expected to drastically reduce the average duration of completed insolvency cases, which was considered to be a major issue under the old insolvency regime (ISET Policy Institute, 2023[19]). However, it is important to note that monitoring activities appear to be fully externalised. Although the government actively participated in the assessments conducted by ISET, its involvement was limited and it had no ownership over the analysis.

In terms of measures to prevent insolvency, although a systematic and institutional approach has not yet been adopted, some relevant initiatives are in place. For instance, a web guide for businesses[4], developed by the EBRD in partnership with Enterprise Georgia (EG) and the Rural Development Agency, provides advisory services and generic guidance to Georgian SMEs experiencing financial difficulties. Moreover, the Business Rehabilitation and Insolvency Practitioners Association (BRIPA), founded in November 2018, offers legal advice to businesses facing financial difficulties and fearing failure, including via the hotline service INSOLAID.

To conclude, Georgia would benefit from adopting initiatives to promote a second chance for bankrupt entrepreneurs. Although there are no formal barriers for bankrupt entrepreneurs to make a fresh start, there are no explicit incentives either, no dedicated strategy is in place, and there are no information campaigns or relevant programmes to promote entrepreneurial second chance.

## *Pillar B: Entrepreneurial human capital*

### *Entrepreneurial learning*

Since the 2020 SBA assessment, there has been a significant shift in the co-ordination of policies related to entrepreneurial learning in Georgia. Previously, an inter-agency working group created by the Ministry of Education and Science, held this responsibility. However, since 2021, most of its functions have been transferred to the newly established Skills Agency. This agency, through a partnership between the ministry and the Georgian Chamber of Commerce and Industry (GCCI), aims at promoting the development of modern skills, inclusive vocational education and the internationalisation of human capital development policy through public-private partnerships. The Skills Agency is also focused on developing entrepreneurial competences.

Entrepreneurial learning is currently included in several policy documents in Georgia, and benefitted from a dedicated action plan, which is a considerable improvement since 2020. The *Action Plan for the Implementation of Lifelong Entrepreneurial Learning at All Levels of Education 2019-2020*, however, has

not been updated since 2020, resulting in the absence of a separate policy document that specifically co-ordinates entrepreneurial learning in Georgia. This direction is now incorporated within the *Unified Strategy for Education and Science 2022-2030* and the *SME Development Strategy 2021-2025*, and their related action plans. The *Unified Strategy for Education and Science* emphasises the importance of supporting the development of creative and entrepreneurial skills among teachers, pupils, students and adult learners across all levels of education. In line with the strategy's 2022-2024 Action Plan, entrepreneurial learning is considered in introducing renewed entrepreneurial modules within all vocational education programmes and updating training curricula to strengthen entrepreneurial skills and competences in higher education institutions.

During the assessment period, the Georgian government took several steps to promote entrepreneurial learning, primarily through the vocational education system. This included supporting the development of educational institutions, updating entrepreneurship modules, and providing capacity building activities for teachers.

For instance, with the support of the United Nations Development Programme, and in co-operation with the Vocational Skills Agency and the Center for Counseling and Training (CTC), a methodology for the organisational assessment of vocational schools was developed to promote the introduction of internal institutional entrepreneurship. Based on this methodology, a new organisational structure of eight professional educational institutions has been prepared. Further efforts were also provided regarding the harmonisation of entrepreneurial modules in VET programmes with the European Entrepreneurship Competence Framework (EntreComp): in 2019, the ministry launched a project to promote entrepreneurial education through the development of a new training module. The module and supporting materials were revised in accordance with the project-based teaching methods. Georgia also made steps towards fostering innovative learning through the establishment of Fablabs in 14 VET institutions.

Additional progress has been made with regard to teacher training, notably through courses and the Skills Agency's plans to develop teacher networks. Moreover, new regulations are reportedly being developed to stimulate VET teacher partnerships and school-to-school co-operation, with the aim to shift the centralised training system to a more co-operative and practice-based model.

However, Georgia's approach to entrepreneurial learning could be complemented by additional activities to promote it in general schools. While significant progress has been made in developing entrepreneurial learning in vocational education, there has been comparatively little advancement in incorporating this approach into general and higher education, resulting in not all students engaging in practical entrepreneurial experience. The Fundamentals of Entrepreneurship module is optional for schools, and entrepreneurial courses are primarily offered in business and technology faculties at the tertiary level. Further efforts are required to ensure more systematic development of entrepreneurship across the country's university network. There is notably a lack of collaboration between general schools and SMEs, and career guidance services remain underdeveloped and rather fragmented, although a Strategy 2022-2026 has been developed to address this issue.

Moreover, policies provide for the assessment of students' learning outcomes, and students are tracked after graduation, but teacher competences on entrepreneurship are not formally evaluated. Overall, data on the development of entrepreneurial learning in schools and higher education institutions is limited; Georgia would therefore benefit from a systematic assessment and collection of statistical data to better evaluate policy development.

In the future, Georgia could further promote entrepreneurial learning in general educational institutions, including entrepreneurship key competence at all education levels, helping students in general schools engage in practical entrepreneurial experience, encouraging non-formal learning and improving career guidance services. Business-school co-operation could also be stepped up between general schools and SMEs, but also strengthening industry-VET school linkages. Indeed, only 18% of Georgian firms had employees with VET backgrounds in 2022, and only 3% of businesses co-operated with VET schools –

although 8% expressed the need and/or wish for collaboration in the short-term (Labour Market Information System, 2022[20]). Georgia could also further develop teacher training on entrepreneurship by including entrepreneurship as a compulsory topic in pre-service teacher training, developing courses in in-service training for teachers in general and higher education, and expanding such learning opportunities to schools'/university managers. Finally, monitoring and evaluation could be improved, notably through data collection and evaluation of teachers' competences to ensure training impact. Recommendations from the monitoring and evaluation of previous policies should feed into the development of new policy documents.

### *Women's entrepreneurship*

Women's entrepreneurship policies in Georgia are enhanced by multiple policy documents, initiatives, and a strong institutional framework, although there have not been any significant policy changes since the last SBA assessment. The establishment of the Sub-Council of Women Entrepreneurship Promotion under the Private Sector Development Advisory Council (PSDAC) in 2017 has served as a platform for strengthening public-private dialogue in this area. The sub-council's primary objective is to identify and address issues related to women's entrepreneurship and develop relevant recommendations.

Georgia has adopted a new SME Strategy for 2021-2025, which includes, for the first time, a dimension dedicated to women's entrepreneurship, and appears as the main national document promoting the development of women's entrepreneurship in Georgia. Additionally, the *State Concept on Women's Economic Empowerment* and the *Rural Development Strategy 2021-2027* recognise the importance of promoting and supporting women entrepreneurs in Georgia. The SME Strategy is, however, the only policy document that defines concrete objectives and activities to support women's entrepreneurship.

Women entrepreneurs benefit from various support programmes, primarily implemented by Enterprise Georgia and GITA. They have been well represented among the participants of Enterprise Georgia's "Micro Grants" and GITA's small grants programmes, with the share of female beneficiaries amounting to 50% and over 30%, respectively, in 2021. Additionally, since 2021, Enterprise Georgia has started accounting for female founders and directors in the Industrial Component Programme, with plans to further improve statistics. The agency also launched a pilot programme to integrate economically inactive women into society in selected municipalities, stimulate the involvement of women in agricultural activities and improve their socio-economic status. Information sessions and e-commerce training were organised for women entrepreneurs. The Rural Development Agency (RDA) has also been supporting agricultural entrepreneurs, including women beneficiaries, e.g. through specific support for the establishment of greenhouses by women. These efforts are complemented by the very active involvement of the private sector on this topic. Business associations and international organisations, for instance, have implemented several initiatives, such as UN Women's project "A Joint Action for Women's Economic Empowerment in Georgia" (JAWE), carried out with the support of two partners: the Business Leaders' Federation "Women for Tomorrow" (W4T) and the GCCI. Through this project, the GCCI actively works with the private sector, government agencies and women entrepreneurs, offering guidance to businesses on how to promote gender equality and women's empowerment in the workplace, marketplace, and community.

Moreover, Georgia has provided policy efforts to reduce women's participation in the informal economy: in 2021, the Gender Equality Council conducted a survey on "Women's participation in the shadow economy and the impact of COVID-19" and developed policy recommendations for relevant institutions to tackle informality among women, still to be monitored. Additional surveys have been conducted on women entrepreneurs in the country, thereby helping to identify persisting challenges women encounter when running a business.

However, according to GEOSTAT's Gender Statistics Annual Report 2022, there has been little change in women's entrepreneurship indicators over the last year. In 2020 and 2021, only 30% and 29%, respectively, of newly established enterprises were owned by women, compared to 59% and 58% for men.[5] This percentage has not changed since 2018. Furthermore, women remain concentrated in low-

value-added sectors, notably in education, human health and social work activities. Women entrepreneurs continue to face significant challenges, including a lack of access to financial resources. Women tend to own fewer assets than men, and their responsibilities related to unpaid domestic and care work, as well as gender stereotypes, create additional barriers to entrepreneurship (UN Women, 2021[21]).

Despite the good participation rate of women in these state support programmes, several challenges remain. A thematic inquiry by the Gender Equality Council emphasised that support programmes did not consider the structural barriers faced by women. Specifically, these challenges include insufficiently active mechanisms for mobilising applicants, a lack of emphasis on motivating potential female applicants, complex application procedures, a lack of consulting and training services for entrepreneurs after financing, and, most importantly, minimal support in selling manufactured products (Gender Equality Council of the Parliament of Georgia, 2019[22]).

Moving forward, Georgia could complement its policy approach to women's entrepreneurship by developing women-specific programmes, which remain at a rather nascent stage in Georgia – yet gender-tailored support would help address the specific barriers faced by women. Further efforts could be provided to support women entrepreneurs outside the capital city, beyond the initiatives of the Rural Development Agency. Co-ordination should be ensured among existing initiatives, and awareness of the support available raised. Finally, strengthening data collection on gender-related issues would be a major step forward – e.g. by enriching databases with more sex-disaggregated data, systematically monitoring, and evaluating the impact of support programmes, and conducting regular surveys on barriers to women's entrepreneurship.

### *SME skills*

The main policy development with regards to SME skills lies in the establishment of the Skills Agency in 2021 by the Ministry of Education and Science of Georgia and the GCCI (see Box 12.2). As a public-private partnership, the agency is in charge of strategic co-ordination in the Georgian VET sector and appears as a key contributor to the national skills intelligence. The Skills Agency has notably developed seven sector skills organisations (SSOs) so far with a view to better understand business skills needs in each sector and tackle remaining mismatches between skills demand and supply.

The Labour Market Analysis Division within the Economic Policy Department at the Ministry of Economy and Sustainable Development, established in 2017, continues to play a central role in collecting and analysing data on SME skills intelligence at the national level. The Labour Market Analysis Division annually undertakes the Survey of Business Demand on Skills, which provides valuable, up-to-date insights into employees' skills, in-demand occupations, human capital development in enterprises, professional education, and more. These surveys target either the entire economy or specific economic sectors: comprehensive economic studies are conducted every two years, while sectoral studies, a new addition since the last SBA assessment, are carried out the years in between. The findings of the surveys sometimes serve as a basis for developing short-term training programmes and are reflected in national policy documents. Moreover, the data collected on in-house training in firms offers interesting information – regarding digital skills, for instance, data show that they gained in importance during the COVID-19 pandemic, with the share of ICT skills trainings tripling between 2020 and 2022, from 4% to 12%.

Georgia has also made further progress in developing its smart specialisation approach, and is currently working towards applying smart specialisation to the country's research and innovation (R&I) policy. The Ministry of Regional Development and Infrastructure, in co-operation with the European Commission's Joint Research Centre, is in charge of this process, and a broad national S3 team has been formed, gathering experts from the main ministries, agencies for R&I and business support as well as international donor organisations. Notably, the Vocational Education Department at the Ministry of Education and Science and the Skills Agency are also members of the working group. Imereti was selected as the pilot

region for mapping economic and innovative potential and the respective smart specialisation strategy is currently being developed. According to the government, the document is projected to be finalised in 2023.

With regard to training provision, several public and private stakeholders, such as Enterprise Georgia, GITA, and the GCCI, provide training for SMEs. These cover various topics, including digital and greening skills. In addition, Enterprise Georgia developed an online training on the basics of export as a response to the COVID-19 pandemic, which increased the demand for remote courses. However, training provision could be stepped up, by widening the range of topics covered, further developing online training, implementing digital learning methods and raising awareness of the support available. Indeed, since there is no systemic structure for developing training programmes for SMEs in Georgia, having a “one-stop shop” for SME trainings could help firms navigate between the different offers. Moreover, Georgia should develop targeted training for SMEs in the areas identified as priorities for smart specialisation Finally, monitoring and evaluation practices could be improved by collecting SMEs’ feedback on training, including testing the acquired competences and capturing the impact of training on their performance. Certification of skills acquired, notably digital ones, could also be beneficial.

### Box 12.2. Georgia's Skills Agency

In 2021, Georgia's Skills Agency was established through a public-private partnership between the Ministry of Education and Science and the Georgian Chamber of Commerce and Industry (GCCI). The agency's mission is to develop skills aligned with the country's economic needs, promoting inclusive vocational education and individualised development, and enhancing public-private partnerships. The Agency is responsible for implementing VET programmes, enhancing the competitive environment, and supporting innovative learning in the country.

The Agency is notably responsible for:

- supporting and co-ordinating VET standard development/update process, including learning material and guidebooks, and of a VET student assessment tool;
- co-ordinating the parties engaged in work-based learning process (private sector, educational institutions, sectoral associations/organisations) and in awarding qualifications;
- providing consulting/training/capacity building to VET institutions and teachers, including to develop re-training programmes;
- supporting career guidance services in VET;
- conducting needs identification and surveys, and participating in monitoring and evaluation;
- developing and introducing a VET communication strategy.

In this regard, the Skills Agency actively supports the formation and operation of sector skills organisations (SSOs) in various sectors of Georgia's economy. These SSOs are crucial for addressing skills gaps and workforce development. Collaboration among key players within each sector is encouraged, and SSO start-up/SSO initiative groups are facilitated to elaborate and revise qualifications, including entrepreneurship-focused competences. Currently, seven initiative groups have been formed in sectors such as tourism, ICT, agriculture, artisan, construction and engineering, wine, and sports.

To enhance digital literacy, the Skills Agency is also working on an IT literacy catch-up course designed for young people and adults, including ethnic minorities with lower digital literacy levels. An e-platform is being developed to facilitate technology-based learning at the vocational education level. The Skills Agency is charged with assessing labour market characteristics, demanded qualifications and skills, as well as employers' future workforce needs using standardised research methodology and instruments. It regularly conducts labour market mini-surveys and gathers data on VET graduates who have completed a mandatory ICT course to identify SMEs' skills needs and bridge the gap between skills demand and supply.

The Skills Agency aims to create a unified research platform where data collected from different research studies can be compared and shared, leading to an aggregated database. This database will provide valuable insights to all beneficiaries, including SSOs, assisting them in revising or developing new qualifications based on the demand for future skills.

Source: (Ministry of Education and Science of Georgia, 2023[23]).

## *Pillar C: Access to finance*

### *Legal and regulatory framework*

Access to bank credit in Georgia is supported by a well-developed legal and regulatory framework. Currently, reforms are underway to provide a legislative framework for competitive factoring market and through general secured transactions framework to improve the acceptability of movable assets as collateral, which should provide another boost for lending, especially to those companies that cannot rely on buildings or land. The reforms aim to improve registration of such assets as well as enforceability to encourage banks to accept assets such as vehicles, equipment or intellectual property as collateral. These are expected to address issues raised by banks around the scope and types of movable security that can be accepted, as well as the enforcement of security rights (BEPS III).

The country's regulatory framework is aligned with Basel III core principles and efforts have been made to curb dollarisation. There is no mandatory disclosure of risks related to foreign exchange borrowing, but capital requirements are set so as to encourage lending in local currency, and rules for small loans in local currency mean that households and smaller SMEs have access to mainly GEL-denominated loans. Given banks' high reliance on deposits for their funding, it was important to encourage deposit dollarisation, which has been supported by the launch of a deposit insurance scheme in 2018 as well as capital incentives on deposits in local currency. As a result, both loan and deposit dollarisation have decreased since 2019.

Since 2018, Georgia has also made the most significant progress among EaP countries when it comes to non-financial disclosure requirements and the introduction of a green taxonomy. The National Bank of Georgia (NBG) has developed ESG Reporting and Disclosure Principles aligned with international best practice. In 2022, the NBG published a Sustainable Finance taxonomy and related classification and reporting regulation obliging banks to classify loans as green, social or sustainable according to the developed taxonomy. In addition, from 2023, commercial banks are required to report on green loans on a monthly basis. The NBG also published a climate-related Risk Radar to assess the climate vulnerability of different economic sectors in the country and apply those to banks' portfolios. Current work revolves around strengthening the National Bank's capacity for climate scenario analysis. ESG issues were also integrated into the Corporate Governance Code for issuers of Public Securities, as adopted in December 2021 by the NBG (entered into force on 1 January 2022). Along with other requirements, the code sets out that companies should implement sustainable development goals, including with respect to environmental and social governance. In relation to the securities market, the NBG has been working on a draft rule on ESG Bond Status. The rule would establish standards to obtain and maintain the designation, set reporting requirements, and determine eligible verifiers who provide pre- and post-evaluation of the debt security's status. The draft regulation is primarily based on the Sustainable Finance Taxonomy of the National Bank of Georgia.

Georgia's capital market is still at an early stage of development, and currently bonds are the market instrument most utilised by companies. The corporate bond market (including local and foreign currency denominated bonds and excluding bonds issued by IFIs) represents around 2.6% of GDP according to 2022 estimates. In part aided by the EU funded Capital Market Support Program, which covers costs for bond issuances, an additional GEL 461 million (EUR ~160 mln) in local- and foreign-currency-denominated corporate bonds were placed on the local capital market in the first half of 2023. The investor mix in those issuances is also diversifying. While GEL denominated corporate bonds are dominated by commercial banks, other investors have become more active. For instance, since 2022, the Pension Agency has participated in bond purchases and is expected to become more active once amendments to the "Funded Pension Law" are adopted by the Parliament. The envisaged changes would increase its concentration limits on a single issuer from 10 to 20 percent. Compared to the bond market, the equity market is rather shallow, with no separate market for lower-capitalisation firms; overall, the stock market does not currently represent a viable financing option for smaller businesses. To boost activity on the capital markets, the

Ministry of Economy and Sustainable Development of Georgia (MoESD), along with Enterprise Georgia, is working on a new programme that will cover the costs associated with bond and equity issuances.

*Sources of external finance for SMEs (bank financing, non-banking financing, and venture capital)*

In recent years Georgia's loan-to-GDP ratio has dropped quite significantly, from a high of 79.9% in 2020 to just around 64% in 2022 (World Bank, 2022[24]). However, in absolute terms, bank lending has expanded rapidly, with an average CAGR of around 15% over the period 2017-2022, resulting in a relatively high banking sector assets to GDP ratio of 98% as of 2022. This suggests that penetration levels in the country have deepened. And indeed, in the last Business Environment and Enterprise Performance Survey (BEEPS), the share of firms using bank credit to finance investments increased from less than one-quarter in 2013 to more than one-third in 2019 (EBRD, 2020[25]).

Lending terms have also become more favourable, with interest rates for SME loans decreasing and only a relatively narrow spread between interest rates for large firms and SMEs. Collateral requirements have more than halved over the past 10 years, probably owing to a better framework for secured transactions and the expanded credit guarantee scheme.

Public financial support programmes are mainly provided through the national agency Enterprise Georgia. These include interest rate subsidies for loans and leasing in priority sectors such as manufacturing and tourism, as well as accompanying grants. Additional support for a wider range of firms was made available during the COVID pandemic. The pandemic also led to the government's relaunch of the national credit guarantee scheme and a significant expansion in 2020, increasing the amount of loans guaranteed fivefold. The scheme continues to be in place and provides guarantees for loans up to GEL 5 million (EUR ~1.75 mln). Supported by international donors such as EBRD, specific support for green investments is also available through Green Economy Financing Facilities that provide finance and advice for investments in green technologies and energy efficiency. Although interest rate subsidies and grants are often only a second-best solution to support broad-based access to finance (compared to, for example, credit guarantees), programmes in Georgia include design features that aim to reduce certain risks typically associated with this type of support. Regular monitoring and sunset mechanisms (such as maximum duration, amount, and number of times a single company can participate) reduce the risk of public funds being misused or spent on low impact endeavours.

Non-bank financing options are available, and partially also delivered through commercial banks (e.g.leasing and factoring). As of June 2023, there were 34 microfinance institutions (MFI) operating in Georgia that account for less than 3% of financial sector assets (National Bank of Georgia, 2023[26]). The sector has gone through a period of consolidation since the last assessment, when more than 60 MFIs were active in the country. This happened alongside major regulatory and supervisory changes that aimed at steering the sector toward more responsible lending and strengthening supervision. However, MFIs are not allowed to take deposits, which constrains their development toward a more rounded finance provider that could serve SMEs and agribusinesses and thus support financial inclusion. However, a new Law on Microbanks was adopted in 2023 allowing for the creation of a new type of financial institution – a microbank – which is supposed to fill the gap between commercial banks and MFIs.

Leasing is offered by some banks but is not subject to a specific regulatory or licensing regime. Similarly, factoring is offered only by commercial banks and focuses mainly on the domestic market, with a penetration rate of 1.2% of GDP. A draft law for factoring has been developed with support by EBRD and is expected to be adopted by the Parliament of Georgia in late 2023. The draft law covers a wider range of factoring types, including reverse factoring, and will be complemented by a modern registry to further catalyse the market. Overall, these reforms strive to establish a fair and competitive marketplace for factoring transactions.

Venture capital and private equity remains nascent, and the legal framework is based on the Law on Investment Funds adopted in 2020. Georgia's Innovation and Technology Agency (GITA) is providing support to help with the establishment of an eco-system conducive to start-ups and innovation activities. Among a range of activities, GITA also provides Innovation Grants for Regions and Startup Matching Grants for early-stage start-ups, but larger-scale funding solutions to attract or amplify private investment are still missing, although there are plans to put additional support mechanisms in place that will provide financing for start-ups at a more developed stage. There has been increased activity in the sector in recent years which can form a good base for further development. 500 Global, a Silicon Valley-based venture capital firm, launched an accelerator programme in collaboration with GITA and Bank of Georgia, making Georgia the hub for their outreach into Eastern Europe, the Caucasus, the Baltics and Central Asia. The programme has run four rounds, bringing together start-ups from Georgia and the wider region, with a call out for a fifth batch to start later in 2023. Besides that, Axel, a Georgian angel investor association, has been established and has invested GEL 1.2 million (EUR ~420 000) to date. In addition, Isari Ventures established a USD 5 million venture capital fund targeted at the Georgian market in 2022.

To support the development of private equity more generally, the MoESD together with the World Bank are working on an instrument to support private equity investments into SMEs with growth potential. Government participation will be in line with amendments made to the Law on Securities Market in spring 2022 which allow the government to participate as a limited partner (LP) in investment funds, capped at 25% (and with no influence over investment decisions).

### *Financial literacy*

The National Bank of Georgia carried out an assessment of financial literacy of the general population in 2016, resulting in the adoption of a National Strategy for Financial Literacy. The assessment did not look at financial skills of entrepreneurs, although the strategy included some actions aimed at SMEs. In January 2023, the NBG adopted a new National Strategy for Financial Education which now recognises SMEs as a target group.

A number of training programmes are available for entrepreneurs. First launched in 2018, the NBG, together with the Development Facility of the European Fund for Southeast Europe and the Export Development Association, developed a financial skills programme for micro and small enterprises that includes training, guidelines and webinars to help small-scale entrepreneurs deal with financial matters, including accounting, financial decision-making, dealing with financing providers and digital payments. In addition, a new financial education website, FinEdu, was launched in 2020 and functions as a repository for resources related to financial education and information.

Financial education is also part of the national curriculum, with modules integrated into the subject of Civic Education within the general secondary school track. In 2020, the NBG developed a teacher-training module in co-operation with the Civic Education Teachers Forum and with the support of the German Sparkassenstiftung (DSIK). The training has only been provided through a specific initiative, however, and is not a regular offering.

### *Digital financial services*

The NBG has drafted a Fintech Development Strategy in consultation with private sector stakeholders. In addition, the World Bank is providing assistance for the development of digital tools within the economy. Data protection aspects are covered in the Georgian Law on Personal Data Protection and relate to natural persons only. Under the country's Open Banking regulation, commercial banks have certain data-sharing obligations and must follow rules of data standardisation. The NBG has also put in place an operational resilience framework that includes provisions for outsourcing arrangements and related risk assessments. These outsourcing rules do not put a limit on responsibilities that could be outsourced.

The NBG has a Fintech and Suptech Development Department and deploys emerging methods such as suptech and an innovation facilitator (a sandbox regime, supported by IFC), which to date has been used by banks to test new ways of customer verification. This means that the NBG is using a wide range of tools to find legal and regulatory solutions to issues posed by the digitalisation of financial services. The NBG is also working on a pilot regime for a Central Bank digital currency. However, while wider consultations have taken place for the development of strategies and action plans in the area of digitalisation, the NBG lacks a systematic multi-disciplinary approach to fintech, meaning that other public or private stakeholders are not part of a regular working set up to discuss and validate decisions.

#### *The way forward*

Access to finance and the surrounding legal and institutional framework are well set out in Georgia. De-dollarisation efforts have shown effect and the NBG should continue its efforts in this direction, including by raising more awareness about foreign exchange (FX) risks amongst borrowers, and by developing local capital markets and an investor base that can support long-term local-currency bonds, for instance.

The reform to ease the use of movable collateral should be implemented, as this will be particularly important for smaller firms and those operating in the service sector. When it comes to non-bank financing instruments, finalising the factoring reform and related registry would support the development of this instrument and in turn ease access to working capital finance for SMEs. Reforms should also take into account any potential impediments to supply chain financing (or, reverse factoring) and be mindful of how factoring transactions are accounted for, to encourage their use. The development of larger-scale funding for start-ups (with a view to crowding-in private investment) would be an important step to develop the sector.

When it comes to digital financial services, the development of a framework for better open access to data for financial service providers could help to encourage non-bank actors into a sector dominated by banks. In addition, regulation around digital finance is currently within the sole domain of the NBG, and while they should be a leading force in these efforts, it is important to adopt a multi-disciplinary approach between authorities to ensure that different aspects of digital finance are covered (e.g. anti-trust considerations, data privacy, ICT regulation, or cybersecurity).

### *Pillar D: Access to markets*

#### *Public procurement*

The main development since the assessment for the SME Policy Index 2020 report has been the creation of an independent review body, the Dispute Resolution Council (drc.gov.ge), for handling complaints about public procurement carried out in accordance with the Public Procurement Law (PPL) of 2005 and with the procurement provisions in the law on public-private partnership (Parliament of Georgia, 2018[27]).

Public procurement in Georgia is still regulated by the Public Procurement Law (PPL) of 20 April 2005 and in force since 1 January 2006, as repeatedly amended (Parliament of Georgia, 2005[28]). A new PPL (Parliament of Georgia, 2023[29]), intended to be fully aligned with the EU Directives for public procurement, was adopted by parliament in early 2023 and promulgated by the President on 9 February 2023. However, the bulk of its provisions will only come into force on 1 January 2025 and some will not apply for another two or four years. Also, procurement by utilities is not yet aligned with the EU Directives.

A comprehensive “Roadmap and Action Plan for the Implementation of the Public Procurement Chapter of the EU-Georgia Association Agreement” was prepared in 2015. It is still applicable, but its implementation has suffered delays and it has not been updated. The action plans under the SME Development Strategy of Georgia 2021-2025 do not contain any references to public procurement.

The State Procurement Agency (SPA) remains the main institution at the national level for public procurement. Its functions include regulation (drafting the new PPL and issuing administrative orders complementing the current PPL), monitoring, training, managing centralised purchasing, and operating the e-procurement system. The five members of the Dispute Resolution Council are appointed by the prime minister and work according to rules of procedure adopted by the government (Parliament of Georgia, 2020[]). The independence of the review body has thus been improved, with the intention to raise transparency and increase trust in public procurement.

A range of measures for facilitating SMEs' access to the public procurement market remain in place. The PPL includes the possibility of dividing contracts into lots, requirements for proportionality of selection and award criteria, and an obligation for prompt payments. The SPA has issued specific guidance materials and training for contracting authorities and enterprises for facilitating the participation of SMEs. In addition, suppliers can use the e-catalogue (www.emarket.spa.ge), which is updated quarterly, to present information about their products, indicating CPV codes, models, specifications, prices, warranty periods and delivery locations. As a complement, contracting authorities may now also publish notices inviting any prospective tenderers to provide specific information in response to the requirements in a particular contract to be concluded, using a specialised website of the SPA (State Procurement Agency, n.d.[]). The PPL sets no explicit obligation for timely payment by contracting authorities but public contracts usually prescribe payment within ten days. The stronger emphasis on sustainable procurement in the new PPL is expected to create further opportunities for successful SME participation in the future.

However, the data currently available do not allow determining whether and to what extent these various SME support measures are effective, and why. The information at hand confirms that certain general issues continue to negatively affect public procurement performance, and SMEs in particular. Direct agreement contracts ("simplified procurement" in Georgian parlance) account for as much as 18% of total public procurement value, although details are not readily accessible (this being said, it should be noted that COVID-19 related procurement is reported to account for an important share of the direct agreement contracts). The average number of tenderers per procedure remains low, below two. Almost 30% of the tenders launched failed, were terminated, or did not lead to any contract award.

Among the reasons for this is the large number of contracting authorities, which means that many of the smaller ones do not have staff with the skills and experience necessary for planning, preparing or carrying out procurement in ways that give SMEs a chance to fairly compete on quality and performance. Another reason is that, in practice, the bulk of the procurement procedures carried out use (purchase) price as the first award criterion and allow tenderers to participate who are not duly qualified and whose tenders do not meet the specifications and other requirements. These factors create strong disincentives for serious SMEs to participate in public procurement and lead to less value for money in the use of public funds.

The further improvement of SME participation would thus require continued efforts to address the standing challenges, including: i) complementing the new PPL by an action plan for its implementation and a longer-term strategy for the development of public procurement, including harmonisation with other SME development policies; ii) aligning procurement by utilities with the EU Directives, whether by a separate law or by amending the PPL; iii) amending the e-procurement system so that it functions as required in the EU Directives and to generate more and better, readily accessible public procurement data, including on SME participation; iv) implementing current and future legal provisions on sustainable procurement in ways that emphasise value for money and support SME participation; and v) taking measures to ensure that all procurement officials have the skills to properly apply principles and practices for open, fair, competitive procurement, including better use of the means for raising SME participation.

### *Standards and technical regulations*

Georgia has made much progress in further developing its regulatory system and quality infrastructure (QI). Concerning overall co-ordination and general measures, the country implemented significant reforms

in the market surveillance system on non-food products. Establishing the independent Market Surveillance Agency (MSA) under the Ministry of Economy and Sustainable Development was a significant step in this context (European Commission, 2022[30]). The MSA conducts market surveillance on non-food products in 12 product areas, for which relevant technical regulations have been adopted. Georgia expects that other products will be added to the MSA's mandate as per the Association Agreement (AA)'s approximation agenda. Another accomplishment was that Georgia's accreditation body, the GAC, became a full member and signatory of the MRA (Mutual Recognition Arrangement) and MLA (Multilateral Recognition Arrangement) of the International Laboratory Accreditation Cooperation and the International Accreditation Forum in 2022, respectively (ILAC, 2022[31]).

Regarding harmonisation with the *acquis,* the approximation of national legislation with the *EU acquis* was intensified. The Georgian National Agency for Standards and Metrology's (GEOSTM), European Committee for Standardisation (CEN) and the European Committee for Electrotechnical Standardisation (CENELEC) Affiliate status is another accomplishment (CEN, n.d.[32]). It was approved in 2022 and entered into force in January 2023. Likewise, GEOSTM became an associate member of the European Association of National Metrology Institutes (EURAMET) in 2022, and preparations to become a full member are underway. As of December 2022, Georgia had adopted about 12 000 EU standards and translated selected ones into the Georgian language.[6] Regarding education on standardisation, Georgia has developed a detailed strategy. GEOSTM has also started creating an e-learning platform in co-operation with the Latvian Standard body. In the field of market surveillance, Georgia has introduced a new online database (European Commission, 2022[30]).

Addressing SMEs' access to standardisation, the Georgian government approved the SME Development Strategy for 2021-2025, followed by a joint action plan of various institutions specifying further support and GEOSTM's diligent implementation of targeted measures. The National Standardisation Strategy developed by GEOSTM for 2022-2024 improved the availability of standards for SMEs and stimulated their participation in standardisation activities. A 10% discount rate for SMEs for purchasing standards was adopted by Ordinance of Government of Georgia No. 503 in 2022. The e-academy will also include modules on SMEs, for example, based on CEN-CENELEC Guide 17, "Guidance for writing standards taking into account micro, small and medium-sized enterprises (SMEs) needs". GEOSTM also plans to introduce an organisation-wide evaluation of SMEs' participation in standardisation. Relying on various monitoring activities implemented by GEOSTM's technical committees (TCs), this is a useful next step.

Concerning the digitalisation of standards and technical regulations, GEOSTM synchronised and harmonised the national standards database with those of the CEN and CENELEC. It also started updating its internal procedures in parallel with the development of the last SME Policy Index report. Georgia began to digitise its accreditation services in 2021 and expects its digitalisation system to become fully operational in mid-2023. Continuing the digitalisation of quality infrastructure, particularly in the field of conformity assessment, is an important ongoing task.

### *Internationalisation of SMEs*

Georgia continues to perform well in supporting SME internationalisation.

Promoting export growth, market access and internationalisation of SMEs is one of the main priorities of the SME Development Strategy of Georgia for 2021-2025 (see Priority 4: Promotion of SME export, market access and internationalisation). Enterprise Georgia (EG) is the agency in charge of promoting Georgian SMEs' access to global markets. The Export Division of EG is well staffed and fully operational and offers various instruments to SMEs, including training, organisation of international trade fairs and exhibitions, support in business matchmaking, and co-financing of technical assistance. Some changes have been introduced since the last SBA assessment. At the beginning of 2022, EG started the new Export Assistance Programme which co-finances technical assistance to exporting businesses and aims to eliminate export barriers in beneficiary companies and introduce export incentive mechanisms to facilitate the diversification

of export markets, products and services; identifying sectors and products with high export potential; and stimulating international sales. The programme has three different directions: i) product licensing/certification; ii) branding; and iii) stimulating international sales.[7] Moreover, in 2020 EG introduced more complex and flexible eligibility criteria, to ensure a transparent beneficiaries-selection process.

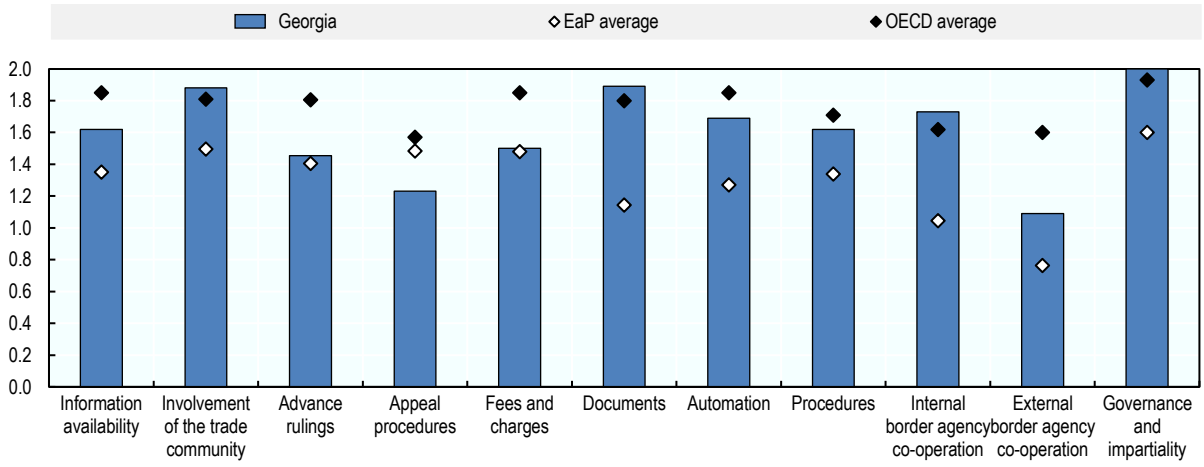
A significant improvement can be observed in Georgia's support for the integration of SMEs into global value chains (GVCs) since the previous SBA assessment. Several efforts have been made to advance Georgia's cluster landscape and several new clusters have emerged, such as the Georgian Construction Materials Cluster, the Georgian ICT Cluster, the Packaging Cluster, the Seed and Seedling Cluster, and the Georgian Apparel and Fashion Association. The MoESD and Enterprise Georgia, in co-operation with GIZ and under the EU-funded Clusters4Development Project, developed a Cluster Policy Framework to create a beneficial cluster landscape and strengthen the internationalisation of Georgian clusters; establish a long-term public-private partnership between industry, academia and the public sector; and promote new clusters in emerging industries (GIZ, 2021[33]). In addition, the Georgian Economic Security Programme 2019-2024 (GESP), launched by the government with the support of USAID, supports economic sectors with the highest long-term potential, helps develop value chains, enhances the viability of SMEs, supports a more skilled workforce, and facilitates public-private partnerships (USAID, 2023[34]). Finally, Enterprise Georgia's Business Universal Programme aims to support the development of business in Georgia and the diversification of domestic production through the creation of new enterprises and expansion and re-equipment of existing ones, and supports key sectors which can then become integrated into GVCs.

Georgia has made considerable progress in the field of policies designed to enhance the use of e-commerce by SMEs. Encouraging and supporting the development of e-commerce is one of the pillars of the NBDS and its associated Action Plan for 2020-2026, and also one of the objectives of the SME Development Strategy 2021-2025 (Objective 5.2). Many initiatives are in place in this field. In 2021, the GCCI implemented a large-scale free training programme for SMEs to raise awareness about the functioning and benefits of e-commerce, with some training specifically targeted at women entrepreneurs. In addition, the Communications, Information and Modern Technology Department at the MoESD is implementing several programmes to promote e-commerce, most of which relate to the development of the necessary infrastructure (for more information on support for the development of infrastructures for the digital economy, see above). A relevant initiative co-ordinated by the same department is represented by the e-commerce pilot between Armenia, Azerbaijan, Georgia and Germany launched in 2021 by EU4Digital to establish national virtual warehouses/databases of local goods to connect e-commerce actors so they can automatically exchange information about sales, customs and delivery (EU4Digital, 2021[35]). Finally, it is important to mention that the MoESD has drafted a Law on E-commerce, which has been submitted to the parliament for adoption. Once adopted, the new law will regulate the rights and obligations of intermediary service providers and online consumer protection, as well as issues related to information disclosure and paid advertisement. There is currently no programme in place to certify that e-commerce companies comply with ethical standards. However, after the adoption of the Law on E-commerce, there is a plan for sectorial association(s), under the co-ordination of the MoESD and with the technical assistance of USAID, to develop a code of conduct identifying and outlining the ethical standards of intermediary service providers.

It is also worth mentioning the outstanding efforts that Enterprise Georgia puts into monitoring and evaluating all its programmes, including those related to SME internationalisation support. For more information on the standardised Impact Assessment Framework developed with the assistance of GIZ see "Support services for SMEs and start-ups" in the next section.

According to the 2022 OECD Trade Facilitation Indicators, Georgia remains the best performer among EaP countries, exceeding or close to the OECD average across several of the assessed areas, such as the involvement of the trade community, simplification and harmonisation of documents, internal border agency co-operation, and governance and impartiality. Some significant challenges remain in the areas of appeal procedures and external border agency co-operation (Figure 12.5).

## Figure 12.5. OECD Trade Facilitation indicators for Georgia (2022)




Notes: EaP: Eastern Partnership. Trade Facilitation Indicators values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade Facilitation Indicators Database, https://oe.cd/tfi.

StatLink https://stat.link/93adsf

In addition to all efforts made so far to facilitate SME access to international markets, there are still some improvements that the government can consider to refine the support provided to small businesses. Moving forward, to facilitate integration of SMEs into GVCs, Georgia could provide further support to importing SMEs and promote technology transfer and the movement of high-skilled workers from multinational corporations. Finally, it is important to ensure that the new Law on E-commerce is adopted and implemented without delay to fill the legislative gaps.

### *Pillar E: Innovation and business support*

#### *Support services for SMEs and start-ups*

Georgia continues to have a strong institutional setting for delivering support services to SMEs and start-ups. The two main government agencies, Enterprise Georgia (EG) and GITA, are well staffed and reportedly dispose of sufficient funding to deliver on their mandate. As such, they are instrumental entities in the implementation of many activities of the ongoing SME Development Strategy. Of particular relevance, in 2023, Enterprise Georgia strengthened its geographical presence in the country, opening three regional growth hubs with the objective to increase awareness of the available support programmes and provide direct training and consulting services to SMEs outside the capital city.

The two agencies offer important financial support programmes for the different segments of the SME population that they serve, which have been expanded since the previous SBA assessment. For micro entrepreneurs, EG offers grants up to GEL 30 000 (EUR ~11 000), with at least 90% of the funding to be directed to capital expenditures. For SMEs, the new programme, *Business Universal*, subsidises interest rates on loan and leasing contracts in the range of GEL 50 000 to GEL10 million (EUR ~18 000 to EUR ~3 million), with at least 50% of the funding to be directed to capital expenditures. In addition, beneficiaries of the programme, under defined conditions, can also access a grant in the amount of 10-20% of the approved loan or leasing. GITA's financial support programmes mostly target start-ups, with the objective to stimulate innovative entrepreneurship; they are described in more detail in the following section.

EG and GITA also engage in the delivery of non-financial support services to SMEs, although progress since the last SBA assessment has been mixed. EG offers technical assistance on developing business

plans, accounting and marketing for the beneficiaries of its micro grants programme, while the co-financing of advisory services is limited to branding and product licensing/certification for export-oriented companies. As regional growth hubs become fully operational, however, it is expected that they will also support SMEs to access a wider range of consulting services (including on business strategy, sales, taxation) by covering up to 90% of the cost. On the other hand, GITA has increased its efforts to develop digital capabilities for the SME sector, focusing its efforts on organising trainings on digital skills for entrepreneurs and IT specialists. Moreover, the GCCI has increased its role as a partner of the government in delivering services to SMEs, in particular through the introduction of a successful training course on e-commerce for entrepreneurs in 2021.

A promising new programme to support SME digitalisation should also be mentioned. As part of the services of the regional growth hubs' services, Enterprise Georgia plans to introduce a set of measures to help SMEs improve their digital skills and adopt digital technologies. With the assistance of digital transformation experts, SMEs first undertake an overall business diagnostic exercise then develop a tailored plan with recommendations on how to digitalise their operations. To facilitate the implementation of such plans, SMEs can apply for financial support to procure digital solutions (up to GEL 25 000 / EUR ~9 000) and train their staff to develop the necessary digital skills (up to GEL 5 000 / EUR ~2 000).

Lastly, Georgia has made very important progress in monitoring and evaluating its SME support programmes. In late 2019, Enterprise Georgia added a dedicated department on analysis, monitoring and evaluation, which looks at all of the services the agency provides. Of particular interest, with the assistance of GIZ, the department developed a methodological framework to rigorously analyse the impact of its support services on its beneficiaries' business performance, which goes as far as attempting to estimate the economic additionality of the agency's services. Starting in 2022, the results of this analysis are published in a report published on the agency's website. In 2023 GITA also established a dedicated analysis, monitoring and evaluation department and is currently developing analytical framework, data observatory and software solutions that will track progress of every GITA beneficiary and outline the impact of respective GITA programmes.

Moving forward, the government should carefully assess the impact and sustainability of the recently inaugurated growth hubs before opening new ones. Building on Enterprise Georgia's experience, GITA could also finalise its analytical frameworks to assess the impact of its support programmes on its beneficiaries. Lastly, in developing its new digitalisation support initiatives, Enterprise Georgia could consider incorporating digital skills development programmes directed specifically to managers of SMEs, who have actual capacity, responsibility and decision-making power to drive the digital transformation of their businesses.

### Box 12.3. Enterprise Georgia's Impact Assessment Framework

Established in 2014 under the Ministry of Economy and Sustainable Development, Enterprise Georgia (EG) is the key government institution responsible for business support, export, and investment promotion in Georgia. Over time, EG has put increasing emphasis on its monitoring and evaluation activities, with the creation of a dedicated Analysis, Monitoring and Evaluation department and the adoption of a comprehensive Impact Assessment Framework, with the aim of moving beyond the "simple" monitoring of activities and rigorously evaluating the economic and social impacts of its programmes and services.

The methodological approach rests on three main pillars: i) a strong "theory of change" for the support programmes, illustrating the logical nexus between activities and expected impact; ii) key impact-oriented indicators describing targets and against which measuring progress; and iii) microdata to analyse firm-level performance. About the latter, EG relies both on primary data obtained through questionnaires among beneficiaries and internal databases of the agency, and on secondary data requested from various external sources, such as the National Statistics Office of Georgia; the National Tourism Administration; the National Bank of Georgia; the Service for Accounting, Reporting and Audit Supervision (SARAS); and the Revenue Service.

A key element of EG's impact assessment is the comparison of its beneficiaries' performance with appropriate benchmarks and via estimation techniques accounting for pre-existing factors affecting company's performance. For instance, key indicators (e.g. revenue, assets, profitability) are tracked for both the "treatment group" (EG beneficiaries) and the "control group" (the corresponding sector of the economy) for several years before and after the implementation of a given EG programme. The estimated impact of a given EG programme is then calculated as the difference between the projected values of an indicator and its actual values in the treatment group.

According to recent EG analysis, for every Georgian Lari (GEL) of co-financing provided by EG, beneficiaries generated additional 14 GEL (EUR ~5) in revenues, contributed additional 4.2 GEL (EUR ~1.5) to GDP, and provide additional 1.5 GEL (EUR ~0.5) in tax revenues per year. In 2021, EG beneficiaries observed a 36% increase in revenue and 22% growth in assets, while the corresponding SME segment's revenues and assets increased by 22% and 12% over the same period, respectively. Interestingly, EG addresses the findings of its impact assessment reports to the government, providing a key input for the design of future support programmes and strengthening the important feedback loop between policies and economic outcomes.

Source: (Enterprise Georgia, 2023[36])

*Innovation policy for SMEs*

The overall policy framework for innovation in Georgia has not evolved substantially since the last SBA assessment (e.g. no national innovation strategy has been adopted), although several strategic policy documents introduced in the last four years contain specific measures for promoting innovation in Georgia. The government's Development Strategy – Vision 2030 – includes the support of science, innovation and technology as one of its priorities; the Unified National Strategy of Education and Science 2022-2030 aims to develop a knowledge-based society and economy-oriented science, research, technology and innovation system; specifically for SMEs, one of the chapters of the ongoing SME Strategy is dedicated to promoting electronic communications, information technology, and research and development. Beyond this, innovation policy in Georgia is regulated by the 2016 Law on Innovations, which establishes legal grounding for the development of the innovation ecosystem (e.g. defining business

incubators/accelerators, determining IP rights) and provides a legislative foundation for financing innovation activities.

Georgia's Innovation and Technology Agency (GITA) is the main implementing body for the development of the innovation ecosystem. With a strong focus on start-up development and the IT sector, it offers a wide range of services to foster innovative entrepreneurship, such as financial support measures, training opportunities, technology transfer programmes, business accelerators and incubators, and techno parks. Over the period under consideration, GITA expanded its physical infrastructure and opened two new techno parks (now eight in total). Moreover, it has partnered with the international business accelerator "500 Global" to offer technology-oriented start-ups an intensive programme to develop their business plan, network with investors, and receive mentorship and training. As part of this co-operation, in 2022, 500 Global established the "500 Georgia" venture fund (USD 20 million), of which GITA has become a partner with a 25% commitment.

One interesting development for Georgia is the first technology-transfer pilot program (TTPP) carried out by GITA in 2019-2022. The programme was supported by the World Bank and the European Union to identify scientific outputs with high commercial potential and assist the research teams in negotiating licensing and business deals with potential business partners. Through this initiative, GITA received applications from several universities and research centres, eventually selecting nine projects with strong potential for commercialisation and international expansion. Although the TTPP ended in 2022, GITA opened two new rounds of applications in November 2022 and March 2023, which serves as evidence of the government's willingness to continue supporting linkages between the local research community and the industrial sector.

Government financial instruments to support innovation have recently been expanded, but remain heavily focused on providing direct grants, tailored to the needs of the different segments of the SME population. In 2023, GITA launched the "Innovation Grants for Regions" initiative, a new initiative replacing the previous "mini grants" programme and offering grants (up to GEL 25 000 / EUR 10 000) to 40 innovative start-ups in Georgia's regions every year, aiming at tackling inclusiveness challenge of innovation activities, which are typically concentrated in the capital cities. Further, the "Start-Up Matching Grants" Programme (up to GEL 150 000, or EUR ~54 000, with 10% private co-financing) aims to stimulate innovation and enterprise creation through the development of innovative products and services with the potential for internationalisation. Lastly, until 2022, GITA provided the "innovation matching grants" programme (up to GEL 750 000/EUR ~270 000, with 50% co-financing) that targeted larger SMEs engaging in a portfolio of projects with the ambition to introduce product, technological or process innovation on a global scale. The programme was abolished in 2022 and GITA is currently designing equity financing programmes and mechanisms that will address the existing financing gaps for start-ups. Indirect financial incentives to simulate investment in innovative activities remain largely unavailable and are not specifically designed for SMEs.

Moving forward, Georgia could consider presenting relevant analysis and policy measures in a unified strategy for innovation policy. With the end of the TTPP, Georgia should also build internal capacity to successfully continue its efforts to advance technology transfer. Lastly, indirect financial support to incentivise investment in research and development and innovative equipment beyond the IT and start-up sector could also be considered.

### *SMEs in a green economy*

The framework for environmental policies related to SMEs has been updated since the previous SBA assessment. First, the SME Development Strategy 2021-2025 now includes the "Development of the Green Economy for SMEs" as one of its seven strategic directions, with specific actions to develop eco-tourism, eco-innovation, and access to green finance. Second, a new Agriculture and Rural Development Strategy 2021-2027 includes measures fostering farming and forestry, as well as supporting the adoption

of efficient and renewable energy technologies in rural households and enterprises, the majority of which are micro and small. Lastly, the Fourth National Environmental Action Programme (NEAP4) identifies the environmental priorities for the years 2022-26, although its implementation calls for more emphasis on SME-related activities, as the document covering the previous period did (NEAP3).

Some incentives have been introduced to help Georgian businesses shift towards renewable energy sources. The Law on "Promoting the Generation and Consumption of Energy from Renewable Sources", adopted in 2019, defines incentive schemes (e.g. "green certificate") for companies to transfer to green electricity consumption and generation. Similarly, the National Energy and Water Supply Regulatory Commission adopted rules for the issuance of certificates of origin of electricity generated from renewable sources, which allows consumers (including SMEs) to choose the origin of their energy, receiving the status of "green companies" and empowering them to contribute to Georgia's energy transition.

The scarcity of green financing has been mentioned as one of the obstacles to SMEs' green development, even though donor-funded initiatives (e.g. the EU's "Promoting Green Lending in the Eastern Partnership" programme) contribute to bridging this gap. The NBG's development of the Sustainable Finance Taxonomy in 2022 is an important development in this regard, which provides a classification system for identifying activities that deliver on climate, green, social or sustainability objectives and is expected to create a framework for green companies to be easily identifiable and have easier access to concessional loans financed by green funds and development banks. In a similar vein, the NBG's Corporate Governance Code for Commercial Banks sets the requirements for environmental, social and governance (ESG) reporting and disclosure, but reporting requirements on firm size will be needed to track the impact of policies to promote green finance for SMEs. ESG issues were also integrated into the Corporate Governance Code for issuers of public securities, adopted in December 2021 by NBG, and requiring companies to report on environmental and social governance aspects, thus contributing to the progress towards the Sustainable Development Goals.[8]

## The way forward

While Georgia stands out for leading its EaP counterparts in SME policy progress, there remains room for reinforcing its policy frameworks for SMEs through the following measures:

- Central to Georgia's efforts to strengthen its digital economy is the adoption of a comprehensive National Digital Strategy (NDS), with clear goals, resource allocation, and task distribution. The NDS should encompass provisions for the digital transformation of SMEs in non-IT sectors. Simultaneously, establishing robust monitoring and evaluation methods for tracking the implementation of the NDS is crucial. In addition to the considerable efforts already provided by Georgia to improve broadband connectivity, the country should further foster competition, investment, and innovation for faster, affordable Internet to consumers and SMEs alike. With regard to digital skills, Georgia could integrate digital competence into all educational levels (backed by teacher training) and strengthen its overall approach by introducing a standardised digital competence framework for assessment and certification, while complementing existing skills assessment and anticipation tools with digital skills components. Establishing a National Digital Skills and Jobs Coalition involving all stakeholders would enhance co-ordination and peer learning with EU countries.
- Georgia could further strengthen its institutional framework by fostering deeper collaboration and good practice exchange between Enterprise Georgia and GITA, for instance in the area of Monitoring and Evaluation or by harnessing their combined efforts to bolster SME digitalisation and the advancement of the ICT sector. The Georgian government should formulate tailored strategies for targeted sectors like tourism and ICT, creating an environment conducive to growth. Furthermore, Georgia should both update the e-Georgia strategy to encompass SME-relevant

Digital Governance principles and adopt the Digital Governance Strategy 2023-2026, while making use of the Digital Governance Agency for streamlined state electronic services. The simplification of the operation environment for business should continue its trajectory of reducing licenses and permits, and expand electronic license management for heightened flexibility, efficiency, and transparency. Company registration processes, known for their advancement, should be maintained, and refined further. Tax compliance procedures for SMEs must sustain preferential taxation for micro and small enterprises, and explore additional simplifications in tax administration, including the implementation of the TDR reform. To improve the support to SMEs to prevent and face insolvency, Georgia should adopt a dedicated strategy and specific initiatives to promote second chance for bankrupt entrepreneurs.

- On entrepreneurial learning, Georgia should complement its current approach by integrating entrepreneurship as a key competence at all educational levels, strengthening teacher training on entrepreneurship, promoting practical experience for students, bolstering non-formal learning opportunities, and enhancing career guidance services. Additionally, business-school co-operation could be stepped up between general schools and SMEs, but also strengthening linkages between industry and VET schools. Monitoring, evaluation, and data-collection efforts should be improved, notably on teachers' competences. To bolster women's entrepreneurship, dedicated support programmes would be useful, notably in rural areas and to help women entrepreneurs scale up, along with improved co-ordination of existing initiatives and enhanced data collection for informed decision-making. For SME skills, Georgia could step up the range of trainings offered, including online ones and in priority areas for smart specialisation, while implementing digital learning methods and incorporate tools to certify the acquired skills. Moreover, Georgia could build on its impact evaluation process by gathering feedback on training, assessing skills gained and capturing the impact on firm performance.
- The NBG should persist in its efforts towards de-dollarisation, raising FX risk awareness and fostering local capital markets. Georgia should also focus on implementing movable-collateral reforms and finalising the factoring reform and a related registry. In doing so, the country should consider supply-chain financing obstacles and encourage factoring transactions accounting. Scaling up start-up funding to attract private investment is also pivotal. Finally, Georgia should develop a framework for better open access to data for financial service providers and adopt a multi-disciplinary approach between authorities, expanding the mandate on regulation around digital finance beyond the NBG to other bodies to guarantee considerations on antitrust, data privacy, ICT, and cybersecurity.
- To further enhance SME participation in public procurement, continued efforts are needed to address key challenges. These include complementing the new Public Procurement Law (PPL) with an action plan for implementation and a long-term strategy for public procurement development, aligning it with other SME development policies. The e-procurement system should be amended to fully align with EU Directives and improving the quality and accessibility of public procurement data, particularly related to SME participation. Measures should also be taken to equip all procurement officials with the necessary skills to effectively apply principles of openness, fairness, and competitiveness, while also optimising methods for increasing SME engagement. Georgia's robust support for SME internationalisation could be enhanced by boosting support for SME imports, promoting technology transfer, and facilitating the mobility of high-skilled workers from multinational corporations. Swift adoption and implementation of the new e-commerce law is advisable to effectively address existing legislative gaps.
- Prior to expanding the recently established Growth Hubs, Georgia's government should assess their impact and sustainability. GITA should finalize its monitoring frameworks, building on Enterprise Georgia's expertise to evaluate the effectiveness of its support programmes. For digitalisation support, Enterprise Georgia could integrate targeted digital skills development specific for SME managers, in order to better equip them with knowledge and skills to drive their

businesses' digital transformations. In the area of innovation policy, Georgia could consider presenting relevant analysis and policy measures in a unified strategy for innovation. With the end of the TTPP, Georgia should also build internal capacity to successfully continue its efforts to advance technology transfer. Lastly, indirect financial support to incentivise investment in research and development and innovative equipment beyond the IT and start-up sectors could also be considered. To further promote SME greening, the NBG's Corporate Governance Codes could include reporting by firm size in order to track the impact of green finance policy on SMEs, while ESG integration into the Corporate Governance Code for Public Securities could also contribute to SDG advancement.

## Table 12.5. Roadmap for policy reforms – Georgia

| |
|---|
| **Strengthening framework conditions for the digital transformation** |
| • Adopt National Digital Strategy, including measures to promote the digital transformation of SMEs in non-IT sectors. |
| • Establish monitoring and evaluation mechanisms for the NDS' progress. |
| • Foster competition, investment, and innovation to support faster Internet at lower prices. |
| • Enhance consumer access to broadband service information and quality. |
| • Incorporate digital competence as a key skill in all educational levels, coupled with relevant teacher training. |
| • Introduce a digital competence framework for assessment and certification, in line with DigComp. |
| • Integrate digital skills aspects into existing skills assessment and anticipation tools. |
| • Establish a National Digital Skills and Jobs Coalition to enhance co-ordination across public and private stakeholders and peer exchange with EU countries. |
| **Enhancing the institutional and regulatory framework and operational environment for SMEs** |
| • Ensure strong coordination between Enterprise Georgia and GITA, fostering synergies for SME digitalisation and ICT sector support. |
| • Explore sector-specific strategies for co-ordinated development in areas like tourism and ICT. |
| • Finalise the approval of the 2023-2026 Digital Governance Strategy. |
| • Enhance agency coordination for seamless public data exchange and interoperability. |
| • Strengthen cybersecurity to mitigate risks amid regional geopolitical tensions. |
| • Evaluate SME tax rates and assess preferential tax impacts on enterprise growth. |
| • Explore initiatives to promote a second chance for bankrupt entrepreneurs, including incentives and dedicated programmes. |
| **Fostering entrepreneurial skills and women entrepreneurship development** |
| • Integrate entrepreneurship as key competence across all levels of education. |
| • Enhance business-school co-operation and teacher training on entrepreneurship. |
| • Improve monitoring, evaluation, and data collection, notably on teachers' competences. |
| • Develop women-only support programmes to help alleviate the specific barriers faced by female entrepreneurs. |
| • Raise awareness of support available for women entrepreneurs. |
| • Strengthen data collection, monitoring, and evaluation efforts on women entrepreneurs and gender-related issues. |
| • Expand the range of trainings, including online courses, and raise awareness of offers available. |
| • Improve evaluation mechanisms by collecting SMEs' feedback on training, assessing acquired skills and impact on firm performance. |
| • Consider offering certification of competences to foster the improvement of the quality of training. |
| • Develop targeted training in priority areas for smart specialisation. |
| **Facilitating SME access to finance** |
| • Continue de-dollarisation efforts by raising awareness about FX risks and developing local capital markets. |
| • Implement reform to ease movable collateral usage. |
| • Finalise the factoring reform and the related registry to improve working capital access. |
| • Address supply-chain financing obstacles and encourage reverse factoring. |
| • Establish larger-scale start-up funding to attract private investment. |
| • Develop an open data access framework to encourage non-bank participation. |
| • Adopt a multidisciplinary approach among authorities expanding the mandate on regulation around digital finance beyond the NBG. |
| **Supporting SME access to markets** |
| • Develop an action plan and long-term strategy for public procurement, aligning the implementation of the new PPL with SME policies. |
| • Revise the e-procurement system to meet EU Directives and improve data quality. |
| • Train procurement officials for fair, open, and competitive practices, emphasising SME engagement. |

- Enhance SME integration into GVCs by facilitating SME imports, fostering technology transfer and skilled worker mobility from multinational corporations.
- Expedite adoption and implementation of the new e-commerce law to address legislative gaps.
- Continue with regular evaluations of technical regulations and quality infrastructure, and implement appropriate response measures to maintain and further improve their advanced level of development.

**Fostering innovation and business support**

- Assess impact and sustainability of inaugurated Growth Hubs before expanding.
- Build on Enterprise Georgia's experience to finalise GITA's assessment frameworks for evaluating effectiveness of support programmes.
- Incorporate digital skills development programmes in new digitalisation support initiatives, specifically aimed at SME managers to lead digital transformations.
- Consider consolidating relevant analysis and policy measures into a comprehensive innovation policy strategy.
- Develop internal capabilities to continue successful technology transfer efforts.
- Explore indirect financial support mechanisms to encourage investment in R&D and innovative equipment beyond IT and start-ups.
- Develop reporting requirements on firm size within ESG reporting frameworks to monitor impact of green finance policies on SMEs.

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## Notes

[1] For more information on the analytical framework, please refer to the thematic chapter Digital Economy for SMEs.

[2] https://infohub.rs.ge/en

[3] https://reformeter.iset-pi.ge/en.

[4] businessguide.ebrd.ge

[5] The remaining 11% and 13% (for 2020 and 2021, respectively) are unidentified.

[6] Statistics vary a little regarding date and scope, see, for example, SWD(2021) 18 final and SWD (2022) 215, p. 12, LEPL referred to almost 12,000 according to CEN/CENELEC

[7] See https://www.enterprisegeorgia.gov.ge/en/export-support

[8] The code is based on the approach – "Apply or Explain an Alternative", the aim of which is to encourage the wider use of good Corporate Governance practice. The code prescribes the reporting process in detail and introduces the obligation for public issuers to prepare a Corporate Governance report.

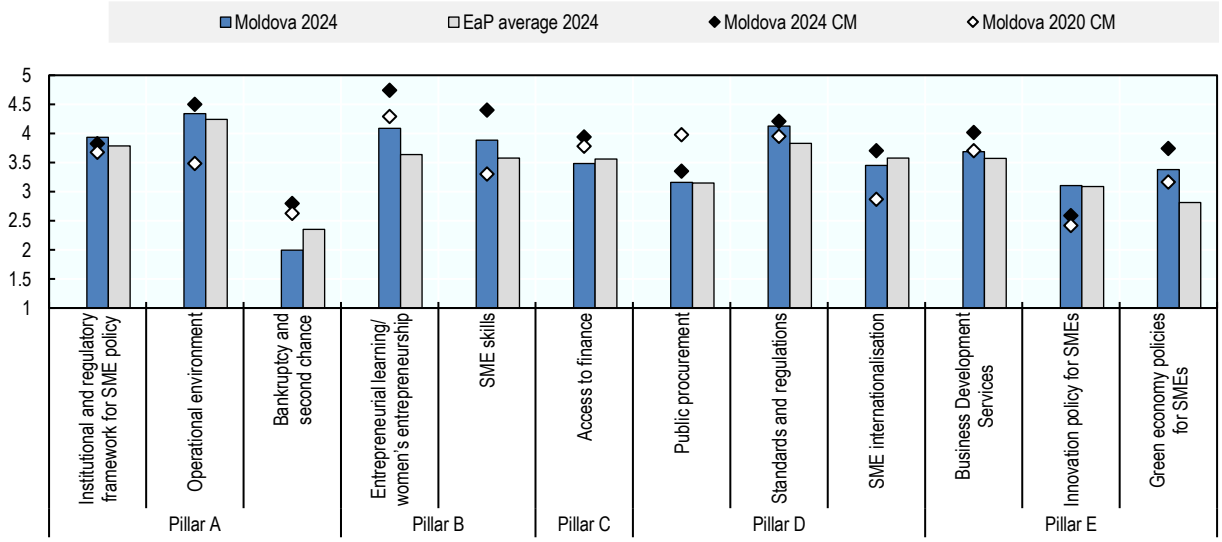
# 13 Republic of Moldova: Small Business Act country profile

This chapter provides an assessment of the progress made by Moldova in implementing the Small Business Act (SBA) for Europe over the period 2020-23. It starts with an overview of Moldova's economic context and dives further into the characteristics of the country's SME sector. It then develops on the state of selected framework conditions for the digital transformation of SMEs. Finally, it analyses Moldova's progress along twelve measurable dimensions grouped in five thematic pillars and sets out targeted policy recommendations.

## Key findings

### Figure 13.1. SME Policy Index scores for Moldova

Country scores by dimension, 2024 and 2020 vs 2024 CM




Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### Table 13.1. SME Policy Index scores for Moldova

Country scores by dimension, 2024 and 2020 vs 2024 CM

| Pillar | Dimension | Moldova 2024 | EaP average 2024 | *Moldova 2024 (CM)* | *Moldova 2020 (CM)* |
|---|---|---|---|---|---|
| Pillar A | Institutional and regulatory framework for SME policy | 3.93 | 3.78 | 3.82 | 3.68 |
| | Operational environment | 4.34 | 4.24 | 4.50 | 3.48 |
| | Bankruptcy and second chance | 2.00 | 2.35 | 2.79 | 2.63 |
| Pillar B | Entrepreneurial learning/ women's entrepreneurship | 4.09 | 3.64 | 4.74 | 4.29 |
| | SME skills | 3.89 | 3.57 | 4.40 | 3.30 |
| Pillar C | Access to finance | 3.48 | 3.56 | 3.94 | 3.78 |
| Pillar D | Public procurement | 3.16 | 3.15 | 3.35 | 3.98 |
| | Standards and regulations | 4.13 | 3.83 | 4.21 | 3.95 |
| | SME internationalisation | 3.45 | 3.58 | 3.70 | 2.87 |
| Pillar E | Business development services | 3.69 | 3.57 | 4.01 | 3.70 |
| | Innovation policy for SMEs | 3.11 | 3.09 | 2.59 | 2.41 |
| | Green economy policies for SMEs | 3.38 | 2.81 | 3.74 | 3.16 |

Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Table 13.2. Implementation progress on SME Policy Index 2020 policy reforms – Moldova

| Priority reforms outlined in the SME Policy Index 2020 | Key reforms implemented to date |
|---|---|
| **Pillar A – Responsive Government** | |
| Upgrade monitoring and evaluation practices in cooperation with the Entrepreneurship Development Organisation (ODIMM).<br>Ensure that regulatory impact analysis (RIA) methodology is systematically applied throughout the public administration.<br>Introduce measures to upgrade the IT skills of small entrepreneurs in parallel with the expansion of e-government services.<br>Upgrade procedures to facilitate online business registration.<br>Implement an early warning system and insolvency prevention training for entrepreneurs.<br>Adopt a comprehensive second chance strategy for bankrupt entrepreneurs. | Establishment in 2022 of the Organisation for Entrepreneurship Development (ODA) as a successor to the ODIMM.<br>Development of the National Programme for Promoting Entrepreneurship and Increasing Competitiveness 2023-2027 (PACC 2022-2026).<br>Adoption of Roadmap on Reducing Regulatory Burdens for SMEs.<br>Development of the RIA "Micro-Enterprise Test" methodology.<br>Inclusion of the digitalisation of company registration in PACC.<br>Design of the Second Chance Programme for SMEs foreseeing the introduction of a digital early warning system for entrepreneurs.<br>Introduction of a simplified bankruptcy procedure with the 2020 amendments to the Law on Insolvency. |
| **Pillar B – Entrepreneurial Human Capital** | |
| Ensure that the European Entrepreneurship Competence Framework features in the 2019-20 curriculum reform plans, backed up with pre-service and in-service teacher training.<br>Improve cross-ministry co-operation to reinforce micro-entrepreneurship for women.<br>Further support small specialisation and vocational education. | Efforts to align the Education Code with European key competences.<br>Education 2030 and PACC to emphasise the role of entrepreneurial and economic education and include actions for the development of learning and entrepreneurial skills.<br>Progress in non-formal learning, e.g. through the introduction of a Framework for Out-of-School Education to stimulate entrepreneurship at all levels of education and the development of regional centres of entrepreneurial education.<br>Development of a *2022 Roadmap on the Economic Empowerment of Women* to foster better co-ordination across stakeholders. |
| **Pillar C – Access to Finance** | |
| Expand credit bureaus' sources of information beyond banks to include utilities and other service providers.<br>Review existing governmental SME support mechanisms, focussing on the more sustainable approaches (such as the recent Credit Guarantee Fund).<br>Pass the draft law regulating venture capital, dormant in the legislative process since 2015. | Expansion of the sources for credit information to include microfinance institutions, leasing companies and other organisations.<br>Launch of the Investment incentive programme "373".<br>Transfer of regulation and supervision regarding non-bank financing institutions to the National Bank of Moldova since mid-2023.<br>Introduction of provisions on venture capital in existing legislation.<br>Creation of a dedicated Fintech division within the National Bank of Moldova in 2022. |
| **Pillar D – Access to Markets** | |
| Increase capacity of Moldovan Investment Agency to deliver export promotion services.<br>Introduce programmes to enhance export readiness of SMEs and support SME-FDI linkages and ensure implementation capacity in the ODIMM.<br>Set up a monitoring and impact evaluation system along with measures to incentivise SMEs to implement EU standards.<br>Develop targeted measures in the field of technical regulations (e.g. online courses for SMEs on how to read and implement standards and translation of standards in priority sectors/products for external trade).<br>Monitor SME participation in public procurement and build contracting authorities' capacity to apply good practices. | Co-ordination of support programmes by ODA and Invest Moldova to support investments and promote exports.<br>Adoption of State Programme for SMEs Growth & Internationalisation to strengthen SMEs' capacity to access foreign markets.<br>Full Membership in the European co-operation for Accreditation.<br>Technical regulation aligned with the provisions of the World Trade Organisation Technical Barriers to Trade Agreement.<br>Adoption of a new regulation for procurement of items below new contract value thresholds. |
| **Pillar E – Innovation and Business Support** | |
| Include specific targets for SMEs in the national strategy for innovation.<br>Enhance the National Agency for Research and Development's (NARD) monitoring system for evaluating economic impact beyond the simple implementation of action plans.<br>Expand the existing co-financing mechanism for SME use of BDS and consider quality certification programmes for private providers.<br>Improve the monitoring and evaluation of current support programmes.<br>Match high-level goals for greening SMEs with measurable indicators.<br>Provide SMEs with information and support to ensure they can benefit from the planned implementation of green public procurement policies. | PACC as a policy foundation for the provision of business support services for SMEs and start-ups.<br>ODA's network of incubators and reorganisation of training offers.<br>NARD's "Innovation and Technology Transfer Project" providing funding for collaborative projects between research and businesses.<br>Introduction of ODA's Programme to Support Digital Innovations and Technological Start-ups awarding grants for different sectors.<br>Greening SMEs as priority of national strategy European Moldova 2030.<br>ODA's Greening Programme for SMEs and Programme for Energy Efficiency supports SMEs' greening policies. |

## Context

### *Economic snapshot*

The Republic of Moldova (Moldova hereafter) has been hit hard by successive crises in recent years. The COVID-19 pandemic, combined witha drought that severely affected the agricultural sector, caused a deep recession in 2020, leading to a GDP decline of 8.3% after a period of steady growth since 2016. While the country recovered in 2021, with growth rebounding to 14% (the highest figure in three decades), Russia's invasion of Ukraine triggered significant shocks for Moldova.

Direct spill-overs from the war heavily affected the country's economy, which contracted by 5.6% in 2022 (Table 13.3) (IMF, 2023[1]). Soaring energy prices raised input costs for manufacturers and led to up to 35% inflation in October 2022 (National Bank of Moldova, 2023[2]), challenging investment and economic growth. External trade initially suffered from sluggish growth in Moldova's EU trading partners and major disruptions, in particular Russia's blockade of Ukrainian ports on the Black Sea. Furthermore, proximity to Ukraine meant that in the first months of the war Moldova faced the extra challenge of welcoming and providing assistance to a large inflow of refugees from Ukraine (more than 115 000 as of July 2023), making Moldova the largest receiver of Ukrainian refugees as a proportion of domestic population. This put additional stress on the country's administrative machine and public finances (UNHCR, 2023[3]). At the same time, the war spurred a wave of solidarity with Ukrainian refugees hosted in Moldova (UN News, 2022[4]) and accelerated the country's European ambitions –bolstered in June 2022 by the granting of official candidate status for accession to the European Union.

In recent years, the ICT sector has been among the locomotives of economic growth for Moldova, its activities generating 5.5% of GDP in 2021 (Statistica Moldovei, 2023[5]). More specifically, according to information presented at the fourth SUM IT UP 4 IMPACT event in Chisinau on 26 April 2023, its export-oriented IT sector doubled its contribution to Moldova's economy and increased its export volume fivefold (EU4Digital, 2023[6]): IT exports jumped from USD 59 million in 2015 to USD 258 million in 2020, which drove most of the rise in the ICT exports from USD 165 million in 2015 to USD 304 million in 2020 (Invest Moldova Agency, 2022[7]). These developments in Moldova's ICT sector accelerated during the COVID-19 pandemic. Moldovan businesses of virtually all sizes started or increased online business activity during the pandemic, with the strongest percentage recorded for small businesses with 69.5%, followed by 67% for medium firms and 60% for large companies (World Bank, 2021[8]). However, the digital transformation of Moldovan SMEs remains at a nascent stage, with less than 17% of them reporting having successfully adopted digital tools in 2020. In this context, it is thus essential that Moldova maintains and strengthens these trends, which bear great potential for supporting SME growth.

**Table 13.3. Main macroeconomic indicators for Moldova (2018-22)**

| Indicator | Unit of measurement | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|
| GDP growth** | Percentage, year-on-year | 4.1 | 3.6 | -8.3 | 13.9 | -5.0 |
| Inflation** | Annual percentage increase, consumer prices | 3.6 | 4.9 | 3.8 | 5.1 | 28.6 |
| Government balance** | Percentage of GDP | -0.85 | -1.47 | -5.32 | -2.62 | -3.26 |
| Current account balance*** | Percentage of GDP | -10.8 | -9.4 | -7.7 | -12.4 | -15.7 |
| Exports of goods and services*** | Percentage of GDP | 30.7 | 31.2 | 27.9 | 30.7 | 41.2 |
| Imports of goods and services*** | Percentage of GDP | 56.8 | 56.3 | 51.3 | 57.8 | 69.3 |
| FDI net inflows*** | Percentage of GDP | 2.3 | 4.0 | 1.3 | 2.8 | 3.7 |
| General government gross debt** | Percentage of GDP | 31.8 | 28.8 | 36.6 | 33.1 | 33.5 |
| Domestic credit to private sector* | Percentage of GDP | 23.2 | 24.8 | 27.9 | 28.7 | 27.7 |
| Unemployment* | Percentage of total active population | 2.9 | 5.1 | 3.8 | 3.2 | 2.3 |
| Nominal GDP** | USD billion | 11.3 | 11.7 | 11.5 | 13.7 | 14.4 |

Notes: GDP: gross domestic product. Government balance corresponds to general government net lending/borrowing; unemployment reflects modelled International Labour Organisation estimates.
Source: * (World Bank, 2023[9]); ** (IMF, 2023[10]) both accessed May 2023, *** (National Bank of Moldova, 2022[11]; National Bank of Moldova, 2023[12]).

### Box 13.1. Moldova's support for SMEs during the COVID-19 pandemic

**Financial support**

The support measures for households and businesses the Moldovan government took during the COVID-19 pandemic accounted for 2.33% of the gross domestic product (GDP), which is relatively low compared to other countries in Central and Eastern Europe (Madan, 2020[13]). The government initiated the value-added tax (VAT) reduction for the hotel, restaurant and catering sector; the deferment of taxing business income for three months; and subsidies to enterprises and non-commercial organisations (Ministry of Economic Development and Digitalization, 2022[14]). Additionally, it set up a programme for firms that took out a loan compensating for their interest payments until the end of 2020 (Ministry of Economic Development and Digitalization, 2022[14]).

**Regulatory flexibility**

In 2020, the government allowed the deadline to be postponed for the 2019 business income tax declaration (Ministry of Economic Development and Digitalization, 2022[14]).

**Workforce support**

As an indirect support measure, the 2020 budget allocated a small share to provide loan guarantees and loans (Madan, 2020[13]). The government also extended eligibility for unemployment benefits and increased the amount of the benefits to a minimum of MDL 2 775 (EUR ~145) (Ministry of Economic Development and Digitalization, 2022[14]).

**Measures to improve access to digital infrastructures**

The implementation of the National Development Strategy (NDS) "Digital Moldova 2020" brought significant improvements on several levels, including broadband connectivity, e-government and the inclusion of digital skills in the education system at all levels of education. Also, a comprehensive SME digitalisation programme was launched in June 2020, notably encompassing a self-assessment test for digital maturity, training and building capacity for over 500 participants, and financial support – grants and business vouchers – that benefitted 168 and 118 companies, respectively (ODA, 2020[15]). The success of the initiative led to the adoption of a follow-up Digital Transformation Programme for SMEs in 2022.

## *SME sector*

Moldova's definition of SMEs adopted in 2016 is in line with EU and international standards. It uses employment, turnover and balance sheet criteria to determine whether a company is a micro, small or medium-sized enterprise. While the employment criteria are consistent with the EU definition, thresholds for turnover and assets are lower in Moldova, reflecting lower per capita incomes.

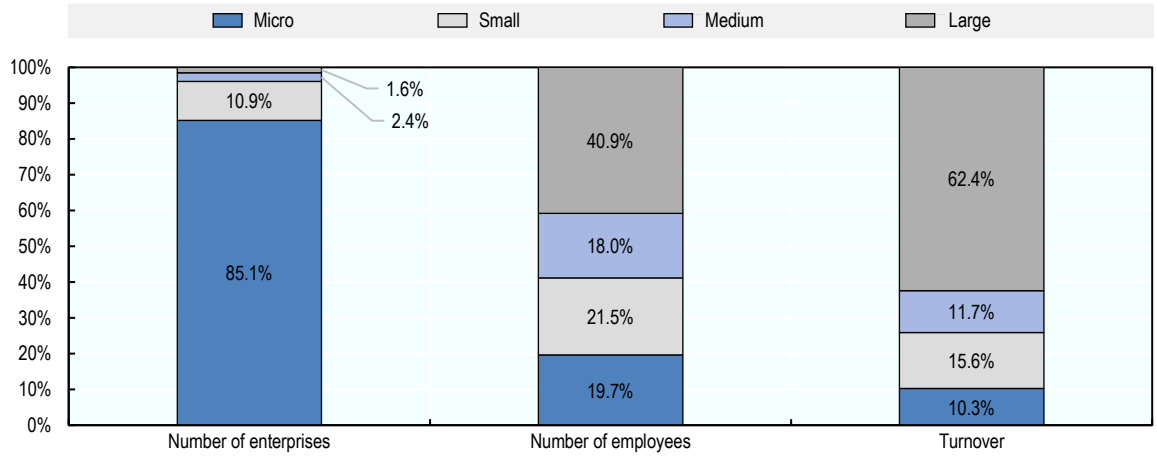
### Table 13.4. Definition of micro, small and medium-sized enterprises in Moldova

| | Micro | Small | Medium |
|---|---|---|---|
| Employment | < 10 employees | < 50 employees | < 250 employees |
| Annual turnover | < MDL 18 million (EUR ~929 185) | < MDL 50 million (EUR ~2 581 070) | < MDL 100 million (EUR ~5 162 140) |
| Total assets | < MDL 18 million (EUR ~929 185) | < MDL 50 million (EUR ~2 581 070) | < MDL 100 million (EUR ~5 162 140) |

Notes: MDL: Moldovan leu; EUR: euro: Exchange rate as of 28 September 2023 (OANDA, n.d.[16]).
Source: Law No. 179 of July 2016 "With regard to small and medium-sized enterprises, modified version.

Some 98% of all firms in Moldova in 2021 were SMEs (59 357 enterprises), accounting for 59% of business sector employment and 38% of turnover. The share of enterprises that are SMEs has remained rather stable in the past few years, whereas their contribution to employment and turnover has been steadily decreasing since 2015 (Statistica Moldovei, n.d.[17]).

## Figure 13.2. Business demography indicators in Moldova (2021)



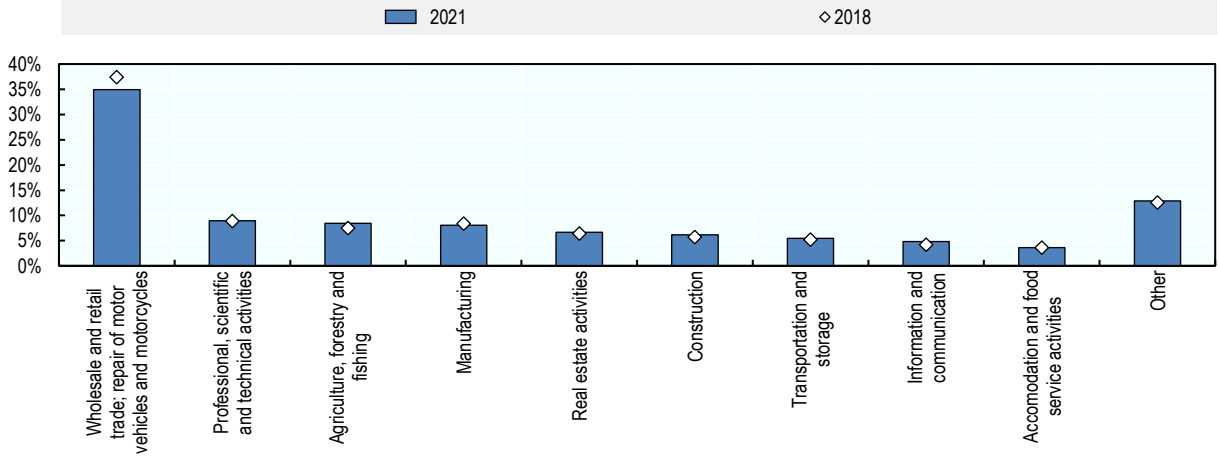

Source: National Bureau of Statistics of the Republic of Moldova.

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SMEs still tend to be concentrated in low-value-added sectors, such as trade and agriculture, although to a lesser extent than in other EaP countries. At the same time, Moldova has the second highest share of SMEs in the ICT sector among countries in the region with 5% of total SMEs operating in the sector in 2021 (Figure 13.3).

## Figure 13.3. Sectoral distribution of SMEs in Moldova (2021 vs. 2018)

Share of SMEs by type of economic activity




Notes: "Other" notably includes mining and quarrying, electricity, gas, steam and air conditioning supply, water supply, sewage, waste management, decontamination activities, financial and insurance activities, administrative and support service activities, public administration and defence, compulsory social security, education, human health and social work, arts, entertainment, and recreation.
Source: OECD calculations based on data from National Bureau of Statistics of the Republic of Moldova.

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## SBA assessment by pillar

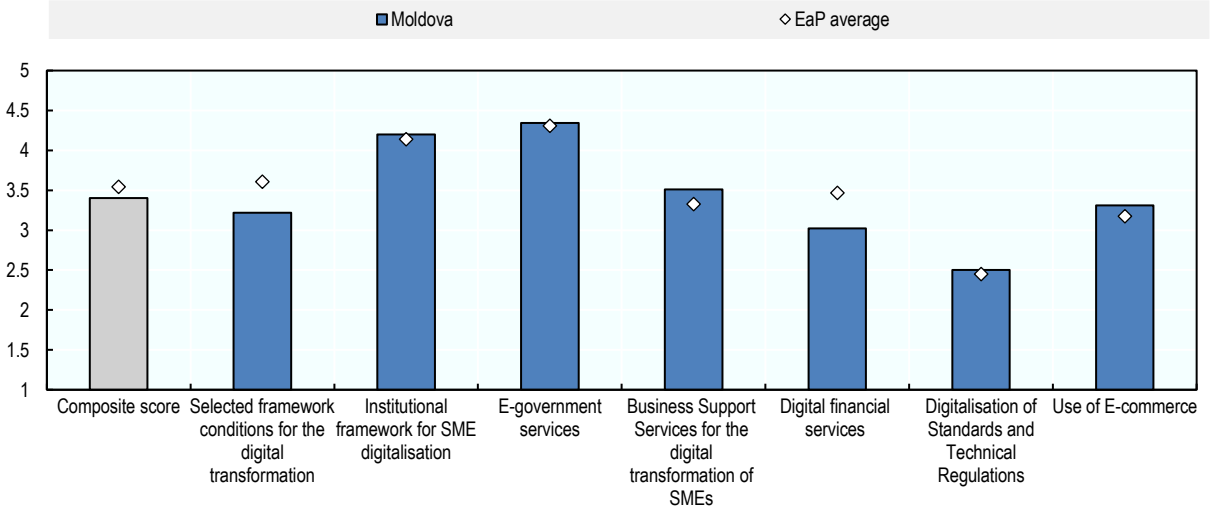
### *SME digitalisation policies*

Creating an environment conducive to the digital transformation of SMEs requires a comprehensive policy approach based on sound framework conditions for the digital economy as well as targeted support to help SMEs reap the benefits of digital solutions. Framework conditions refer to pre-requisites for the digital transformation, such as affordable access to high-speed broadband, a satisfactory level of digital literacy among citizens, and a well-coordinated and coherent policy approach and governance system for digital policies. In the context of SME development, those fundamentals need to be complemented with specific business support services, digital financial services for SMEs, and tailored support to engage in e-commerce to reach new markets.

Reflecting the multi-faceted nature of the topic, this round of SBA assessment evaluates EaP countries' policy approaches to SME digitalisation through i) a dedicated pillar on selected framework conditions for the digital transformation, as well as ii) six new sub-dimensions, incorporated in the pre-existing dimensions of the SBA assessment, to delve deeper into specific thematic policies to foster the digital transformation of SMEs. The weighted average of the scores for the new pillar and digitalisation-oriented sub-dimensions results in a composite score for SME digitalisation policies presented below (Figure 13.4)[1].

Moldova's composite score for SME digitalisation policies of 3.40 revolves around the regional average. The country's digitalisation efforts are reflected in key policy documents, such as the National Programme for Promoting Entrepreneurship and Increasing Competitiveness 2023-2027 (PACC) and the National Digital Strategy, and e-government services are well developed. Moldova also appears among the top performers in terms of business support services for the digital transformation, thanks to its abovementioned comprehensive SME digitalisation programmes. Efforts to develop digital financial services and to digitalise standards and technical regulations remain, however, at a nascent stage. Overall, the limited number of indicators available on digitalisation (e.g. on digital skills) appears as a persistent issue.

### Figure 13.4. Scores for SME digitalisation policies in Moldova




Note: Further details on the assessment and calculation methodology can be found in the "Assessment framework" section in the Digital Economy for SMEs chapter, in the "Policy framework, structure of the report and assessment process" chapter and in Annex A. Additional information on institutional framework for SME digitalisation and e-government services can be found in Pillar A; on digital financial services in Pillar C; on use of e-commerce in Pillar D; and on Business support services for the digital transformation of SMEs in Pillar E.

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The following section details Moldova's performance in developing selected framework conditions for the digital transformation, while more information on digitalisation-oriented sub-dimensions can be found in the sections on the pillars they respectively belong to.

## *Selected framework conditions for the digital transformation*

Individuals and firms, notably SMEs, cannot fully reap the benefits offered by the digital transformation without the existence of robust framework conditions, such as comprehensive digitalisation policies, access to high-speed Internet and well-rounded ICT skills among the population. Accessible, affordable and stable broadband connection is indeed the *sine qua non* for i) ensuring widespread participation of citizens and businesses in the digital economy and ii) stemming the widening of the connectivity gaps between urban and rural territories and between firms of different sizes. Furthermore, fostering digital skills development at all stages of life (through formal education and lifelong learning initiatives for adults) is essential to help the working-age population acquire the skills they need to embark on the digital transformation, produce tech-savvy consumers, and build a talent pool of IT specialists.

### *National digital strategy*

Moldova has made digitalisation a policy priority. It adopted its first national digital strategy in 2013, *Digital Moldova 2020*, which was organised around three pillars: 1) expanding broadband connectivity; 2) fostering the development of digital content and e-services; and 3) strengthening ICT usage capabilities. Building on the previous strategy, the government prepared a new *Digital Transformation Strategy of the Republic of Moldova for the Years 2023-2030*. The concept for this document was proposed for public consultation in December 2022, and the draft Strategy was publicly discussed and officially endorsed during May-June 2023 (Particip.gov.md, 2023[18]). The new document is more ambitious and broader in scope, focusing on six priority objectives: 1) development of a digital society; 2) development of a robust and competitive ICT sector; 3) creating an innovative and resilient digital economy; 4) establishing an efficient, intelligent, and invisible digital state; 5) creating an accessible, safe and inclusive digital environment; and 6) consolidating the image of Moldova as a digital nation. With regard to the business sector, the strategy follows a comprehensive approach, encompassing measures for technology start-ups with international growth ambitions; companies from the ICT sector; and the digitalisation of the traditional sectors of the national economy.

In parallel, Moldova has worked to build an efficient institutional framework for digitalisation. The appointment of a Deputy Prime Minister for Digitalisation in 2021, and the redesignation of the Ministry of Economy as the Ministry of Economic Development and Digitalisation in February 2023, reflect the importance the government attaches to the topic, and are welcome steps to ensuring co-ordination among stakeholders and towards adopting an overarching approach to digitalisation. Building on Moldova's strong track record on public-private partnerships and consultations, dedicated co-ordination mechanisms are being implemented. Public and private actors are regularly involved in the development of draft projects and legislation and, in line with these practices, the new strategy envisages the creation of a dedicated co-ordination body for implementing the measures: the National Council for Digitisation. The council will be chaired by the deputy prime minister for digitalisation and involve public and private sector representatives, including from the ICT industry and civil society. It will have several permanent working groups on the different topics covered by the strategy.

In terms of monitoring and evaluation, the new strategy includes a range of targets for each of the six objectives, with the aim for more than half of Moldovan companies to use cloud/artificial intelligence/big data; over 40% selling their products and/or services online; and at least 60% of SMEs having a basic use of digital technologies. The framework is based on the EU's Digital Economy and Society Index (DESI) methodology.

However, the previous strategy *Digital Moldova 2020* was only partially implemented, with only half of its objectives being achieved. For example, only 12% of public services were available online at the end of the implementation period[2] (compared to the strategy's goal of 100%), and the acceptance rate of electronic public services barely reached 50%, instead of the planned 70% (Government of the Republic of Moldova, 2022[19]). These implementation gaps reportedly reflect a lack of institutional co-ordination and capacity, insufficient funds, poor project and risk management, and ineffective monitoring. Monitoring and evaluation practices have been further impeded by a lack of available indicators to properly assess progress and impact, e.g. on digital skills and SMEs' use of digital tools.

The next steps for Moldova on its digitalisation journey are therefore to i) ensure co-ordination and implementation of the upcoming National Digital Strategy to try and avoid the caveats from the previous one, defining clear roles for stakeholders and allocating sufficient funds; and ii) closely monitor and evaluate impact and develop relevant indicators to assess progress made towards the initial targets (see Table 4.2 in the "Digital Economy for SMEs" chapter for concrete examples).

### *Broadband connectivity*

Moldova does not have a broadband strategy *per se,* but several policy documents – *European Moldova 2030* and the *Radio Spectrum Management Programme for 2021-2025* – include provisions to increase access to high-speed Internet. As a follow-up to the *Radio Spectrum Management Programme 2015-2020*, this new document sets as its main objective the continuous development of the electronic communications industry and the information technology and communications sector in Moldova, including the development of networks and public services of mobile broadband electronic communications. It also entails provisions for radio spectrum resources necessary for the continuous development of a terrestrial mobile broadband electronic communications network.

Moldova currently benefits from one of the highest rates of high-speed broadband connection in the EaP region: 98% of the country's subscriptions are above 10 Mbit/s, vs. the regional average of 75% in 2021 (ITU, 2022[20]). The country has planned additional measures to further improve broadband quality: the *Radio Spectrum Management Programme 2015-2020* sets the target to have 97% of the population with 4G/5G coverage by 2025, also improving data transfer speed (expected to reach 50 Mbps by the end of the implementation period). Moreover, broadband uptake has been fostered by significant improvements in affordability over the past years: prices for fixed broadband per capita almost halved between 2018 and 2020 (from 4.78% of gross national income [GNI] per capita to 2.25%, respectively), and mobile broadband prices per capita dropped, from 2.15% of GNI per capita in 2018 to 0.48% in 2020.

Nevertheless, broadband subscriptions, while above the EaP average, remain, overall, below OECD and EU levels. One-quarter (25%) of the Moldovan population had a fixed broadband subscription in 2021, against 35% in the OECD. The gap is wider for mobile broadband subscriptions, with close to 88 per 100 Moldovans having a subscription, against 108 per 100 in the OECD population. Additionally, Moldova suffers from a persisting digital divide between urban and rural areas, the widest gap across the region: only 58% of households in rural areas have access to the Internet vs. 80% in urban areas. The *Radio Spectrum Management Programme* acknowledges the issue and aims to tackle it. Finally, Moldovan authorities, notably the National Regulatory Agency for Electronic Communications and Information Technology (ANRCETI) and the e-governance agency, collect data through annual surveys to assess the extent of the digital divide – between genders, age groups, and education and income levels. Data on broadband uptake and quality among businesses are, however, not yet available.

Moving forward, Moldova should pursue efforts to reduce digital divides – for example, by further improving the affordability of fixed broadband, as it remains above the International Telecommunication Union's 2% target. More could be done to foster broadband uptake among businesses, and data should be collected to assess digital divides across firms of different sizes, in terms of both number and speed of connections. Finally, broadband policies would benefit from more multi-stakeholder consultations: while policy

documents are submitted for public consultation, regular consultations should be held with network operators, consumers, regulatory authorities and all levels of government, to ensure that all views are considered throughout implementation.

### *Digital skills*

Moldova has embedded digital skills development in several policy documents – the national digital strategies (past and upcoming), the *Strategy for the Development of the IT Industry 2018-2023*, the *Education Code* and *Education Strategy 2030*, and the *Government Action Plan 2021-2022*. These documents vary in terms of focus and target groups: while the *Education Code* mentions digital skills in the list of key skills to be acquired within the educational system, the *Strategy for the Development of the IT Industry 2018-2023* aims to develop competitive human capital in the field of ICT, as the lack of advanced ICT skills is a persistent challenge. The other strategic documents foresee measures to foster lifelong learning of digital skills and to help adults become digitally literate across all regions of Moldova.

As a result of previous policies, digital skills have become a pillar of the Moldovan educational system. Digital competence is a key competence in the national curricula, at all education levels: the module "Digital Education" became compulsory in 2018 in primary schools for grades I-IV, and older pupils continue to gain digital skills through the informatics discipline (mandatory in upper secondary general schools) and other school subjects. In the vocational education and training (VET) system, digital skills training is provided through either a transversal approach or professional studies programmes. The so-called "transversal/cross-cutting approach" focuses on training of basic IT skills, to be tested and obtained through the end-of-studies qualification. The second approach trains students on IT skills through professional study programmes. Higher education institutions are obliged to offer IT courses to first- and second-year students. A number of additional, optional courses have been introduced to develop advanced ICT skills, e.g. on robotics, mobile application design, website development, introduction to IT security, and artificial intelligence.

Efforts to train teachers have contributed to the implementation of digital literacy in the education system. In 2020, the Ministry of Education and Research launched the National Digital Literacy Programme to reduce the digital literacy gap and develop IT skills among teachers. The programme resulted in close to 76% of primary, secondary, and high school teachers being trained in 2020, and 80% of early education teachers in 2021. Additional measures were designed as a response to the COVID-19 pandemic, including the development and dissemination of training materials to teachers, and the launch of online and hybrid study platforms such as *Studii.md*, *Education Online*, and *Învat.Online*.

Digital skills policies benefit from the active involvement of the private sector, which creates additional opportunities: the Moldovan Association of ICT Companies (ATIC) appears as a driving force, offering a wide range of services, such as training courses and awareness-raising campaigns. ATIC also implements one of the flagship public-private partnerships: the ICT Centre of Excellence Tekwill (Box 13.2). In addition to ATIC, several higher education institutions have signed co-operation agreements with businesses to further promote digital skills: the Technical University of Moldova, for instance, is collaborating with Orange Moldova Foundation to further develop professional training and certified courses; facilitate internship opportunities; and extend the Solidarity FabLab, a digital manufacturing education project, to three Moldovans regions. The university also has a partnership with Moldcell to jointly implement a series of academic, research and educational projects.

### Box 13.2. Moldova's Tekwill project

"Tekwill" is an innovative centre and project in Moldova aiming at supporting ICT industry growth, enhancing professionals' skills, and fostering technological innovation and entrepreneurship. Launched in 2017, Tekwill is a collaborative effort involving the Government of Moldova, USAID, the Government of Sweden, Microsoft and IBM. Named after "Tek" for technology and "will" for the future, Tekwill carries out various initiatives to support digital skills development among Moldovans of all ages andsocial and professional backgrounds. It also fosters sectoral collaboration between the IT sector and traditional industries, such as agriculture.

The main activities and objectives of Tekwill include:

- ***Skills Development***: Empowering IT professionals, students, and entrepreneurs via diverse training programmes, workshops, and courses in the ICT field.
- ***Technology Transfer***: Facilitating the transfer of knowledge, expertise, and technology between the local ICT community and international experts, fostering collaboration and innovation.
- ***Entrepreneurship Support***: Nurturing technology startups and entrepreneurs with mentorship, incubation, and acceleration programmes to catalyse business growth and development.
- ***Networking and Events***: Organising conferences, hackathons, and networking events to bring together IT professionals, entrepreneurs, investors, and industry experts, creating opportunities for collaboration and partnership.
- ***Research and Development***: Supporting ICT sector research and development efforts, promoting innovation, and advancing technology within Moldova.
- ***Advocacy and Policy Development***: Advocating for policies and initiatives that fuel the growth and sustainability of the ICT industry in the country.

Tekwill has achieved remarkable success, completing/supporting 878 educational and 499 entrepreneurship initiatives and solidifying its position as a highly successful tech initiative in the region. It has been instrumental in empowering over 472 teams to excel in business, create new opportunities, and attract investment, while also training and orienting over 152,500 individuals.

Tekwill is a driving force behind Moldova's ICT landscape, cultivating innovation, entrepreneurship, and positioning the country as a strong contender in the global technology market. It has played a crucial role in fostering a thriving tech ecosystem, attracting investments, and nurturing a skilled workforce to meet the demands of the rapidly evolving digital world. The initiative is foreseen to be replicated across the country through regional centres, notably in Cahul, Comrat and Bălți.

Source: (Tekwill, 2023[21]); (Moldovan Association of ICT companies, 2023[22]).

However, lifelong learning initiatives remain at a rather nascent stage, and digital skills development among businesses of all sizes could be further encouraged, as this remains a major challenge (see below). This applies to both generic and advanced ICT skills. As highlighted in the draft national digital strategy, while Moldova's education system lays the foundations for advanced professional digital skills, it lacks programmes that attract enough talent, including girls and women, to pursue science, technology, engineering and mathematics (STEM) careers and address the lack of specialised IT skills among the population. This human capital issue is further aggravated by the country's persisting brain drain.

Moreover, co-ordination across ministries and with external stakeholders could be further improved. Moldova involves public and private actors in policy design (e.g. through public consultations with students, parents, teachers, central and local public authorities, non-governmental organisations (NGOs), and partners for the development of the next Education Strategy), but some stakeholders, despite their relevance, have only played a limited role so far – the Ministry of Labour and Social Protection and the National Employment Agency (ANOFM), for instance.

Finally, insights on the levels of and needs for digital skills across Moldovan individuals and businesses remain scarce. Data on digital skills levels are not available, and there is reportedly no assessment of students' progress in acquiring digital competences, nor a framework for the certification of digital competences. There are no anticipation exercises on digital skills needs, apart from some examples conducted by development partners.

Moving forward, Moldova should strengthen its approach to digital skills policies by strengthening its multi-stakeholder approach: it could foster the involvement of the Ministry of Labour and Social Protection and ANOFM (to ensure synergies with labour market policies, e.g. the National Employment Strategy, and implement digital skills assessment and anticipation exercises, building on ANOFM's labour market analyses), and of non-governmental stakeholders, such as employers and teachers. This could be facilitated by the creation of a National Digital Skills and Jobs Coalition, in line with EU4Digital guidelines. Moreover, digital skills development among businesses could be further promoted, especially smaller firms that lag behind large ones in their digital transformation journey. Adopting a digital competence framework to serve as a common reference, such as DigComp (see the dedicated box in the chapter on Digital Economy for SMEs), would facilitate the certification of skills acquired. Finally, Moldova would significantly benefit from improving digital skills assessment and anticipation exercises by collecting data on digital skills levels, ensuring digital skills policies are monitored and evaluated, including digital skills insights in the labour market analyses, and consider adopting additional skills anticipation exercises[3].

## *Pillar A: Responsive Government*

### *Institutional and regulatory framework*

Since the previous SME Policy Index assessment four years ago, Moldova has made significant progress in strengthening the institutional and regulatory framework for SME policy and in aligning policy practices to those of the EU Small Business Act despite the disruptions caused by the COVID-19 pandemic and the impact of the war in Ukraine. Moldova has traditionally placed a strategic priority on conducting regulatory reforms and on improving the operational environment for SMEs. While this approach is still valid, additional priorities, such as supporting SMEs' digital transformation and innovation, now receive more attention as well.

#### Institutional setting

SME policy in Moldova is the responsibility of the Ministry of Economic Development and Digitalization. The Organization for Entrepreneurship Development (ODA) – established in 2022 as a successor to ODIMM – has been tasked with policy implementation.

In An independent evaluation of the 2012-2020 SME Development Strategy was carried out in 2021 by experts financed by the EU Technical Programme for Moldova. It found that approximately 70% of the envisaged actions had been completed. The strategy improved the operational environment, but issues have been highlighted in relation to SME's access to finance and to the way public agencies communicate with the enterprise sector.

The government presented the draft National Programme for Promoting Entrepreneurship and Increasing Competitiveness (PACC) was developed by the government and presented as a draft at the beginning of

2022. However, the COVID-19 pandemic and the war in Ukraine delayed its approval and imposed a revision of some of its objectives. At the end of June 2023, the government was ready to adopt the document, and final approval was expected by the end of 2023.

As mentioned above, in 2022, ODIMM was reorganised into the Organisation for the Development of Entrepreneurship (ODA). ODA retains the same mandate as the ODIMM, dealing with entrepreneurship promotion, the provision of training courses and business advisory services and the management of a Credit Guarantee Fund. The reform is expected to improve the governance of the agency, particularly in relations to its role as provider of credit guarantees, as well as to simplify access to the support to SMEs programmes.

### Legislative simplification and RIA

Moldova has a good track record on regulatory reforms. Under the co-ordination of the Economic Council to the prime minister, the government is currently implementing the “Roadmap on Reducing Regulatory Burdens for SMEs by 2022” and its Action Plan. The documents will serve as landmark documents for the implementation of actions to simplify entrepreneurship activity by introducing a simplified tax regime for SMEs, reviewing labour regulations (particularly for micro enterprises) and state inspections, and developing an RIA “Micro-Enterprise Test” methodology.[4]

According to the Law on Normative Acts (No. 100/2017), RIAs on business-related legislation should be applied across the public administration and policy documents. The State Chancellery, through the Regulatory Impact Assessment Secretariat (SEIR), co-ordinates RIA applications. The methodology was updated in 2019 and is now aligned to EU standards. RIAs were conducted on more than 90% of government-initiated business regulations. Around 100 RIAs have already been performed, covering both legislative acts and regulations. In addition, the SEIR is associated to a working group of independent experts providing methodological assistance to public authorities in conducting RIAs as part the World Bank project "Improving Competitiveness II”.

### Public-private consultations

Public-private consultations are mandatory and are conducted regularly. In line with Government Decision No. 23/2019, every policy initiative that is expected to have an impact on businesses must be analysed by the working group of the Commission on the Assessment of the Impact on the entrepreneurial activity, which includes representatives from the private sector. Moreover, the Law on Transparency in the Decision-Making Process (No. 239/2008) makes public consultations mandatory for all policy initiatives and draft policy documents. The State Chancellery annually reviews the level of transparency of all central public authorities and publishes a “Report on ensuring transparency in the decision-making process of central administrative entities”. The State Chancellery’s latest report on public-private consultations (PPCs), conducted in 2021, specifies that public consultations/debates were carried out on 91% of draft laws and 83% of draft government decisions/ordinances adopted in 2021.

Various civil society organisations also provide independent reviews of the PPC process. Public comments are collected though an e-platform: https://particip.gov.md/ro. Although there has been some improvement since the previous assessment, citizens’ and the associative sector’s participation in public consultations remains relatively low, as indicated by the data below. Out of a total of 2 356 recommendations resulting from PPCs and received by line ministries and other authorities of the central public administration, only 50 (approximately 2%) came from citizens; 541 proposals (approximately 23%) were received from NGOs. Finally, another 456 proposals (approximately 20%) were filed by representatives of the business sector. The global rate of acceptance of the received proposals was 55%. The rate of acceptance of proposals received from citizens and the business sector was only 37%; that of proposals from the associative sector was 47%.

#### Institutional framework for SME digitalisation

The National Programme for Promoting Entrepreneurship and Increasing Competitiveness 2023-2027 (PACC 2023-27) contains specific measures related to SME digitalisation. Those objectives include facilitating the transfer of technologies and innovations, with a focus on IT technologies, as well as supporting the digital transformation of SMEs, drawing on ODA's dedicated programmes. The Organisation has been implementing two digitalisation-specific programmes – one to foster digital innovation and start-ups, and one to accelerate the digital transformation of SMEs in non-IT sectors.

The government is planning to allocate a budget of close to MDL 50 million (EUR ~2.6 million) over the period 202 –25 specifically to a programme supporting SME digitalisation. ODA is in charge of the programme implementation, while the Ministry of Economic Development and Digitalization supervises, monitors programme implementation, and ensures co-ordination with the Digital Transformation Strategy of the Republic of Moldova for the years 2023-30.

#### The way forward

To continue improving its institutional and regulatory framework for SMEs, Moldova should complete ODA's reform by assigning adequate human and financial resources and by structuring its activities in line with the objectives of the new SME Development Strategy. In addition, the country should i) step-up the process of regulatory reform, in order to meet the requirements associated with the future EU accession status; and ii) take actions to bring SME policy guidelines in line with EU requirements (i.e. the SBA annual performance review). Moldova should also measure efficiency of enterprise support programmes' implementation and public agencies' performance, in view of a likely increase in EU technical assistance funding associated with the accession process. Finally, the country should introduce an RIA SME test, monitor SME usage of public procurement (PP) electronic platforms, and take action to increase SME participation in public consultations.

### *Operational environment for SMEs*

Improving the operational environment for SMEs has been a long-standing priority for Moldova. Since 2020 the government has placed a high priority on the provision of e-government services to decrease conformity costs and provide swift and high-quality services for the businesses.

#### E-government services

The NPACC 2023-2027, disclosed for public consultation at the beginning of 2022 contains specific objectives and measures related to the provision of digital services to the business sector. They include: the complete digitalisation of the processes for company registration, suspension, closure and operation of various changes in status; the digitalisation of customs procedures comprising the electronic declaration for all types of customs regimes; the modernisation of the electronic control system to enable risk-based controls and the digitisation and automation of control reports; and the continuous digitisation of government-to-business services (permits, licenses, authorisations, permits, etc.) through the Digital Single Window (Permit Management and Issuance Mechanism).

Efforts have been made to put in place a complete legislative framework for the digitalisation of government services. In 2021, the government adopted a comprehensive legislative act[5] to facilitate remote interaction and government-to-business (G2B), business-to-business (B2B), and business-to-consumer (B2C) digital interactions. The new legal framework allows for remote registration of a company and modification of the businesses' incorporation or liquidation documents. It foresees the possibility of using electronic signatures in employment relations between an employer and an employee, including the signing of remote employment contracts. Moreover, unilateral recognition of qualified advanced electronic signatures issued in EU countries is now granted, allowing the Moldovan diaspora and European investors to interact with

the Moldovan authorities at a distance. The new regime allows for a wider use of electronic documents and strengthens the provisions of the Law on Electronic Identification and Trust Services no.124/2022. In addition, it introduces the digital power of attorney in relations with public authorities and facilitates remote registration on the public procurement portal and, subsequently, for submitting an offer for electronic public procurement. Finally, it facilitates the use of electronic documents in other areas of importance for businesses, including relations with public utility companies (natural gas, electricity, water/sewerage, communications, etc).[6]

The government service MDelivery (Government Decision No. 152/2021), launched in 2022 is a digital platform for disseminating the performance of public services. In February 2023, the Law on Public Services entered into force (No. 234/2021). It sets out the two main concepts underpinning digital government: the "digital-by-default" and the "digital-first" principles.[7] Relying on these principles, public institutions will be obliged to receive electronic documents and give priority to issuing documents in electronic format.

Finally, the MConnect Interoperability Platform was established according to Article 6, paragraph (3) of Law no. 142/2018, which obliges public entities to share data and interconnect their data banks, support interoperability among public institutions.

### Company registration

Company registration procedures, already advanced, have been further simplified. They are now available online and can also be conducted from outside the country. Amendments to Law No. 220/2007 on state registration of legal entities and individual entrepreneurs (Art. 8, (1), a), provide for the possibility of submitting documents for registering legal entities of any kind in electronic format, applying qualified advanced electronic signature (remote authorisations request). If the registration request has been made through a representative, the power of attorney can be issued through the digital platform MPower, a registry of the powers of representation based on electronic signature. All decisions adopted by the Agency for Public Services (state registration body) concerning the incorporation, reorganisation, liquidation, suspension or resumption of the activity of the company, of its branches, as well as changes to its documents of incorporation, can be released electronically. At the same time, some of the taxes for the services provided by the state registration body were eliminated, including the tax regarding drafting, or amending an act of incorporation, decisions of the general assembly of the founders (associates), among others. The specified changes considerably simplify the registration process.

### Business licensing

The licensing process is organised in line with the "one-stop-shop" approach. New amendments to Law No. 160/2011 on regulating through authorisation of entrepreneurial activity were adopted in 2021. The amended law introduces the concept of an "Integrated Information System for Managing and Issuing Permissive Documents" (SIA GEAP). Article 6 (2.2) specifies that permissive acts such as licenses, permits and others, as well as their duplicates, can only be issued, refused, extended, perfected, suspended or withdrawn by the issuing authority through the SIA GEAP. Thus, the processes of issuing such documents were standardised, thereby increasing transparency. In addition, the provisions of Article 6 (2.3), which entered into force in 2022, provide that in all cases, the licenses, permits, authorisations and certificates or their duplicates be issued in the form of an electronic document sent to the email address indicated by the applicant or through the government electronic notification service. If the requested permissive act is produced on paper (physical format), an electronic copy will also be issued. Currently, through this digital platform it is possible to request and issue 86% of permissive documents (131 out of a total of 152).

#### Tax compliance procedures for SMEs

A number of modifications have been introduced since the previous SBA assessment to create a simplified tax regime for individual entrepreneurs and micro and small enterprises. Tax administration procedures have been simplified with the introduction of a one-stop shop electronic platform for tax filing, an e-invoicing system, an e-request for registration as a VAT payer or of subsidiaries, and the launch of the Personal Office of the Taxpayer. The process of easing tax compliance for SMEs is co-ordinated by the Economic Council operating under the Prime Minister's Office. A permanent working group, the Advisory Council for Small and Medium Enterprises, has been established with the mission of identifying key issues, concerns and needs of SMEs in Moldova, including those related to the fiscal administration. The working group includes one member representing the SME sector: the director of the Alliance of Small and Medium-Sized Enterprises of Moldova. There is currently no online portal managed by the Tax Administration to offer tax-related information to SMEs. However, the Fiscal Service has developed a guide – The Taxpayer's Guide for Beginners – that presents the main fiscal aspects for persons wanting to start an entrepreneurial activity.

As part of the process of rationalising the tax regime for individual entrepreneurs and MSMEs although there are no personal deductions or a minimum non-taxable income level for auto-entrepreneurs; some presumptive tax thresholds have been increased, allowing more individual and microenterprises to benefit from the simplified tax regime. For instance, the upper threshold for individuals earning an income from commercial activities and registered as sole proprietors was doubled at the end of 2022 and is now MDL 600 000 (EUR ~31 000). The tax rate in this case is set at 1% of individual income, but not less than MLD 3 000 (EUR ~160).

Corporate income tax is set at a flat rate of 12%. However, SMEs that are not registered as VAT payers and that meet specific criteria stipulated in the Fiscal Code may opt for a special corporate income tax (CIT) regime with a 4% tax rate on aggregate sales determined for accounting purposes.[8] There are also tax incentives for enterprises located in information technology parks. They are subject to a unified tax rate of 7% of total sales revenue. The tax includes corporate income tax and contributions to the Social Fund and the Medical Insurance Fund. Finally, at the end of 2022, the parliament approved an amendment to the tax code introducing a total tax exemption on non-distributed dividends earned by SMEs and a new VAT tax refund system for enterprises not conducting import-export activities.

#### The way forward

Moldova can continue improving SMEs' operational environment by further extending the range of public services available through e-platforms and collecting data on the use of e-government services by SMEs to increase their usage – e.g. by improving SME digital skills and conducting promotional campaigns. To simplify SMEs' tax compliance, the Tax Administration should consider establishing an online portal that offers tax related information to SMEs. In addition, Moldova should calculate the effective tax rate imposed on different types of enterprises and the impact of different tax regimes and incentives on enterprise growth. Finally, the country should conduct surveys of SMEs and consultations with SME sector representatives in order to better modulate the SME tax regime and reduce areas of non-compliance and informality.

### *Bankruptcy and second chance*

Survival and bankruptcy procedures in Moldova are governed by the Law on Insolvency No. 149/2010, recently amended by Law No. 141/2020. The law considers enterprises in distress as entities in need of immediate support to restore and continue their business. It protects the rights of creditors and establishes clear rules for their repayment. The state and government agencies are not given priority over other debtors, and tax debts can be paid in instalments. There are no specialised insolvency courts; insolvency cases are heard by courts of general civil jurisdiction.

The 2020 amendments introduced important changes, including a simplified bankruptcy procedure (accelerated restructuring procedure) and the establishment of an electronic registry for insolvency cases. The simplified bankruptcy procedure aims to preserve the debtor's business as a going concern, maintain employment and satisfy outstanding claims by application of a restructuring plan (Article 218). Under this procedure, the debtor is limited to negotiating a restructuring plan with its creditors that is subject to final approval and confirmation by the court (EBRD, 2021[23]). Although the establishment of the electronic registry is provided for in law, the registry is still under development.

In 2021, within the framework of the DanubeChance2.0 project, co-financed by EU funds (European Regional development Fund, Instrument for Pre-accession Assistance, European Neighbourhood Instrument), the Organisation for Entrepreneurship Development (ODA) carried out several activities related to the elaboration of a national early warning mechanism. More specifically, ODA's staff were trained on how to design and implement an early warning mechanism for SMEs, how to use the online self-diagnostic tool, and how to analyse a company's situation based on financial indicators. However, the DanubeChance2.0 project expired in December 2021 and early warning mechanisms are still not systematically adopted.

Nevertheless, Action 4.7.1 of the Government Action Plan for 2021-2022 refers to developing, approving, and launching the Second Chance Programme for SMEs in line with EU Directive 2019/1023. The programme, designed by ODA, envisages the introduction of a digital early warning system and self-assessment tools for entrepreneurs, as well as mentorship and "first aid" measures for SMEs in financial distress. It also foresees the establishment of the Recovery and Sustainable Development Fund to provide direct financial assistance to SMEs in distress and provides metrics for the impact assessment on preventive insolvency policies targeted at SMEs. However, although the programme has been developed and consultations have been held, it has not yet been approved; it has therefore not yet started to be implemented. Thus, at the moment there is no comprehensive policy framework in place to promote second chance.

Moving forward, the government should consider establishing specialised insolvency courts and proceed with the development of the electronic registry for insolvency cases. In addition, it should further improve the existing measures to support SMEs in financial distress and prevent insolvency. To this end, Moldova could prioritise the approval and subsequent implementation of the Second Chance Programme. Moreover, the government could step up efforts to monitor and evaluate existing programmes and the regulatory framework related to bankruptcy and second chance, as there is currently no established mechanism to assess and ensure the effectiveness of such programmes across all sub-dimensions.

## *Pillar B: Entrepreneurial Human Capital*

### *Entrepreneurial learning*

Over the past two years, Moldova has continued to make progress on a comprehensive approach to entrepreneurial learning by making it one of the pillars of its strategic planning documents. Moldova is currently adopting a new generation of strategies in terms of education and SME development, with the *Education 2030* development strategy and the PACC 2023-2027.

Both draft policy documents contain relevant actions for entrepreneurial learning: *Education 2030* emphasises the role of entrepreneurial and economic education of the young generation and the society to achieve a sustainable and inclusive economy, while PACC 2023-2027 entails nine dedicated actions for the development of learning and entrepreneurial skills

Entrepreneurial learning policies continue to benefit from the involvement of a wide range of stakeholders – general and VET educational institutions, ODA and ANOFM, as well as NGOs and the associative sector.

Starting from a strong base in 2020, Moldova has made further progress during the assessment period. With regard to non-formal learning, for instance, the new Framework for Out-of-School Education in Moldova, based on the Education Code, sets "stimulating creativity, innovation, and entrepreneurship at the level of all components of education" as one of its objectives. A normative-legal framework for non-formal learning was developed and approved, enabling one to validate non-formal and informal education and have their professional skills certified. The government has also stepped up its support to promote entrepreneurial learning through non-formal education in regions, with the development of six regional centres of entrepreneurial education: Chișinău, Ungheni, Leova, Hancesti, Drochia, and Edinet. These centres were set up by the Ministry of Education and Research and USAID.

Furthermore, entrepreneurial learning is still promoted among the general population via various means, including information campaigns, annual events, awards' ceremonies (e.g. the Annual Competition on the Best Business Plan) and success stories of successful entrepreneurs. As for education systems, further progress has been made in implementing digital and innovative learning methods through donor support, including for the development of entrepreneurial skills. Clasa Viitorului, for instance, is a project for the digital transformation of education implemented in Moldovan schools. It consists of a new concept in pedagogy, offering an open and inspirational learning space with interdisciplinary and innovative approaches through the use of digital technologies, which favours the student-centred learning process. VET and higher education institutions have increased their co-operation with businesses, notably though work-based learning – on-site learning/in-school practical training two to three days a week, carried out in most VET institutions; on-the-job training, i.e. internships in companies (for 12-14 weeks), ordinarily in a business unit; and dual education, mainly organised in companies (about 70% practical training and 30% theoretical lessons). The main universities in Moldova have several active partnerships with various companies and organisations in the development of dual education.

Despite this progress, not all learners engage in practical entrepreneurial experience: there are some examples at different levels of education and in various schools, mostly with donor support, but these remain ad hoc. Moreover, while Moldova benefits from good examples of VET-higher education-business co-operation, the co-operation between general schools and SMEs on entrepreneurial learning remains limited. Finally, the impact of the policies implemented could be improved – e.g. by assessing students' progress in learning entrepreneurship as a key competence at each education level and systematically tracking students' labour market outcomes after graduating from some levels of education (presently, this is only partially done, and only for VET and higher education institutions).

Moving forward, Moldova should ensure proper monitoring and evaluation of the upcoming strategies (Education 2030 and PACC), and all activities related to entrepreneurial learning in general, to foster evidence-based policy making and certify that entrepreneurial skills are properly acquired. These documents should also clearly define responsibilities across the many stakeholders involved to ensure co-ordination, concrete implementation and policy efficiency. Finally, building on successful cases of co-operation between VET and higher education institutions, collaboration between general schools and SMEs on entrepreneurial learning could be further developed to foster the development of an entrepreneurial spirit among all students and to help them acquire relevant cross-functional skills.

### *Women's entrepreneurship*

Building on previous efforts, various policies and programmes support the development of women's entrepreneurship across the country. Notably, in 2022, Moldova launched a *Roadmap on the Economic Empowerment of Women*, developed by the Economic Council of the Prime Minister – an action plan which includes a specific chapter on promoting women's entrepreneurship and will foster better co-ordination across stakeholders involved in promoting women's entrepreneurship. A "Familia" programme was also adopted, entailing a range of measures to help alleviate the challenges that women face while pursuing their carrier goals[9]. Moreover, the parliament introduced the "Equal pay for equal work" principle, while

several measures were adopted to support families and facilitate the fair participation of parents in the process of raising and caring for children. Women's entrepreneurship is to be addressed in the upcoming PACC 2023-2027, with the goal of increasing the share of enterprises managed by women from 30% in 2022 to 35% in 2025. The Strategy notably foresees financial literacy and IT courses for women and girls.

In terms of measures implemented over the assessment period, ODA (formerly the ODIMM)'s *Women in Business pilot programme*, approved in 2016, was extended for three years in 2019, being changed from a pilot programme to a full programme. Through training, mentoring and co-financing components, the programme helped over 1,200 women gain managerial skills through business development and increased their access to resources, financing, services and technologies. The Programme expired in October 2022, and its evaluation results, stemming from the interview of over 300 women beneficiaries and outcome indicators, will feed into a follow-up Women's Economic Empowerment Programme, to be approved in 2023. Additional support is provided through non-formal but active co-operation with private actors and NGOs, e.g. the Association of Women Entrepreneurs from Moldova (AFAM) and the Public Association – National Platform of Women from Moldova (PNFM). Besides ODA's programme, several women-specific support initiatives have been successfully implemented, including the *Women's Pre-Accelerator Programmes* (short intensive courses for women who want to start their own businesses), mentoring programmes, and sector-specific support (e.g. in tourism). Women's entrepreneurship is further fostered by awareness-raising campaigns and annual events, such as *THE DREAM GETS WINGS: Shaping the future of women in business*, and more is being done to encourage girls and women to go into STEM education, with a specific National IT Training Programme for Girls and Women.

Nevertheless, more concerted efforts could be implemented to support female micro entrepreneurs in rural areas, as well as incentives to reduce women's participation in the informal economy. Women entrepreneurs could be supported beyond the early stage of business development to ensure the viability of their projects and help them scale up their businesses. The case of Enterprise Ireland offers an interesting example in that regard (see the relevant Box in the Pillar B chapter). Finally, Moldova lacks data insights on women-led SMEs, which constitutes a considerable area for improvement (see Pillar B chapter for concrete examples of indicators that could be collected). Surveys on barriers for women entrepreneurs could also be more systematically conducted to help assess any remaining issues – following the good example of the Analytical Report on the Participation of Women and Men in Entrepreneurship published by the National Bureau of Statistics in 2020.

### *SME skills*

Since the previous assessment, Moldova's SME agency, ODA (formerly the ODIMM), has expanded the already wide range of trainings it was offering to SMEs – now covering new in-demand topics such as the circular economy, internationalisation and digitalisation. It also targets additional groups. One of the milestones in this assessment period is the implementation of ODA's *Program to Support Digital Innovations and Technological Startups*, launched in 2022. The programme aims to develop scalable IT and green innovations, providing non-reimbursable financial support to innovative ideas and targeting a new category of SMEs, i.e. start-ups with growth potential and digital start-ups. ODA also started a support programme for the digital transformation of SMEs in non-IT sectors in 2020 (see Box 13.1), which was successfully renewed in 2022, as digital competences remain the most in-demand skills among Moldovan SMEs. The agency also introduced online trainings to ensure continuous support during and after the COVID-19 pandemic.

Moreover, SME skills are analysed within the different projects implemented by ODA. The agency monitors and evaluates its support programmes, collecting participants' feedback through questionnaires assessing their level of satisfaction and knowledge gained and using the information it gathers through the surveys to make adjustments. In addition, the National Employment Agency (ANOFM) conducts annual labour

market analyses based on a survey of firms of different sizes, providing insights into persisting skills gaps in the country and feeding into the policy-making process.

However, although data on SMEs' participation in training are collected (disaggregated data by sex and region), the government does not evaluate their impact on SME performance. There is no large-scale evaluation of SME skills, resulting in a lack of data on managers' and employees' skills. There is also no evaluation on the barriers to SMEs' participation in training. Indicators on firms offering in-house training and firms employing IT specialists, for instance, are also unavailable. Skills anticipation practices remain at a nascent stage, limited to the ANOFM's annual surveys.

With regard to smart specialisation, Moldova has made progress since the previous SBA assessment towards adopting the "smart specialisation" approach, notably through the *National Programme in the Fields of Research and Innovation for the Years 2020-23*. Following the mapping process, four areas of specialisation were identified for Moldova: 1) energy; 2) ICT; 3) agriculture and the processing of agricultural products; and 4) biomedicine, biopharmaceutics and bioinformatics. An inter-ministerial working group was created, gathering a broad range of public and private stakeholders (Ministry of Education and Research, Ministry of Infrastructure and Regional Development, Ministry of Finance, Ministry of Economy, Ministry of Agriculture and Food Industry, Ministry of Health, Ministry of Environment, National Agency for Research and Development, ODA, research and innovation agencies, development partners, and sectoral business associations and NGOs operating in the priority areas). The group drafted a dedicated strategy, which was proposed for public consultation and is awaiting approval.

Moving forward, Moldova could build on this progress and improve its approach to data collection; impact evaluation; and skills assessment and anticipation tools. It should adopt a systemic approach to data collection on SME skills, needs and in-house training, publishing the results on an online database. It could also further develop skills anticipation tools: the methodology of the labour market analyses could be strengthened, for example by offering longer term projections (e.g. for the next three, five and ten years); broadening the pool of surveyed firms to improve the representation of micro, small and medium-sized businesses; and using the same questions over time to allow for comparability between years. Skills-needs studies of selected sectors could also be considered. In terms of monitoring and evaluation, Moldova could improve its approach by assessing the impact of trainings on SME performance. ODA could also consider collecting feedback on skills acquired through its online platform, and further develop digital learning methods. The agency could also step up its efforts to support digital skills development among small firms, as the lack thereof remains a major challenge – for example, by extending the range of topics covered by digital skills training, offering certification of competences acquired on the basis of a digital competence framework, raising awareness of the available training, and encouraging peer learning and on-the-job training.[10] Finally, the approach to smart specialisation could be enhanced by designing and implementing targeted training for SMEs in the identified priority areas. Involving the Ministry of Labour and Social Protection and ANOFM could also be beneficial, given their prominent role in labour market policies.

## *Pillar C: Access to Finance*

### *Legal and regulatory framework*

Moldova continues to have a well-established legal framework for secured transactions, regulated through the Civil Code. A cadastre with online accessibility is in place. In 2019, a register for movables covering different types of assets was established and is available online. This should help companies with insufficient immovable assets obtain a loan as it reduces uncertainty around movables. However, usage of movable assets is still not very widespread. In a survey of commercial banks conducted by the EBRD in 2022, seven out of nine respondents indicated that the availability of immovable collateral was an important or very important aspect in their lending decision to SME customers, whereas for movable assets only three banks stated that this was an important factor. The same survey also suggests that

enforcement remains an important issue, with more than half of surveyed banks stating that enforcement of security rights over immovable and movable assets is inefficient (EBRD, 2021[24]).

The expansion of sources for credit information in 2021 was an important reform to boost access to finance in Moldova. Information is now collected not only from banks but also from microfinance institutions, leasing companies as well as other organisations, such as utility providers and telecommunications companies. This significantly broadened the coverage of credit information in Moldova from a very low base of only 18.2% before the reform to over 60% of the population today (World Bank, 2020[25]).

Banking regulation and supervision have received significant attention in the context of an International Monetary Fund-led review following the 2014 banking crisis. Authorities have made substantial progress in rehabilitating the banking sector since then. The regulatory and supervisory framework has been strengthened and the National Bank of Moldova (NBM) is set to assume regulatory authority over non-bank financial institutions to enhance overall financial sector oversight. Basel III core principles have been implemented. Within this framework, the risk weight for SMEs has been adjusted downward to encourage SME lending. At the same time, foreign currency (FX) lending to unhedged borrowers (many of whom tend to be SMEs) is regulated through a number of prudential requirements, including stricter credit classification, limits on overall FX exposure and disclosure requirements around the risks of FX borrowing in order to mitigate related risks. Nevertheless, FX exposure in the banking sector has remained significant, with nearly a third of loans extended in foreign currency.

Commercial banks are not currently subject to specific disclosure requirements related to environmental, social or governance (ESG) standards and risks. Similarly, climate-related stress testing has not yet been introduced into the central bank's regulatory toolbox and a green taxonomy does not yet exist. These measures are important to consider given the increasing importance of ESG standards for doing business, as well as the potential risk that climate change poses for banks' portfolios. The Strategic Plan of the NBM for 2023-2025 recognises this and sets an objective of developing a regulatory and supervisory framework for green and sustainable finance. In agreement with the IMF, the NBM intends to integrate climate risk assessments in its supervisory framework and plans to issue guidance for banks and other financial institutions on the governance, management, reporting and disclosure of climate-related risks. Together with building capacity to monitor climate risks, these changes should enable the NBM to conduct and publish climate stress testing. In addition, the International Finance Corporation (IFC) is supporting the NBM in developing a sustainable finance roadmap.

The local capital market only has a limited degree of sophistication. For instance, the Moldovan Stock Exchange is characterised by a low level of issuances, transactions and trading volume, all of which have been trending downward since the last assessment. (Moldova Stock Exchange, 2023[26]) Only a few entities are listed (13 in the regulated market and 20 in the alternative trading system) and the market is quite illiquid. (National Commission for Financial Markets of the Republic of Moldova, 2023[27]) As of June 2023, only three government bonds have been issued and no corporate ones. It, therefore, does not constitute a viable alternative financing option even for SMEs, even those at the larger end of the SME definition.

### *Sources of external finance for SMEs (bank financing, non-banking financing, and venture capital)*

Bank financing is the single most important external funding source for SMEs. The banking sector crisis of 2014-15, which led to the liquidation of three banks at a cost of 10% of GDP, significantly affected the extension of private credit. Domestic credit to the private sector as a share of GDP plummeted from an already low level of 36% in 2013 to 23% in 2017. Since then, credit penetration has only recovered slightly, and remains below pre-crisis levels (World Bank, 2022[28]). These low levels are also reflected in banks' balance sheets, where gross loans amounted to only 41.6% of total banking sector assets as of June

2023. As of 30 June 2023, bank finance to SMEs amounted to MDL 18.3 billion (EUR ~950 million), a decrease of 3.7% compared to the end of 2022, representing 29.6% of total loans (also a lower share than end-2022).

The ODA is the key provider of support for SME access to finance. Two instruments are particularly important: the Credit Guarantee Fund (FGC) and the newly launched investment incentive programme "373". A comprehensive range of complementary training and assistance programmes aim to provide a holistic support infrastructure for SMEs under one roof.

The Credit Guarantee Fund (FGC) provides guarantees to a range of businesses, including start-ups, young and women entrepreneurs, and export-oriented businesses, among others. Guarantees are extended on the basis of loan applications with commercial banks, covering 50-80% of the loan amount. As noted in the last assessment, the Moldovan government has significantly expanded the programme in recent years, first increasing the number of guarantees from 27 to 116 between 2018 and 2020, then quadrupling it to 468 in 2021. These increases were further supported by a decision of the National Bank of Moldova (NBM) resulting in more favourable risk weights for loans that benefit from a guarantee provided by the FGC (National Bank of Moldova, 2018[29]). The increase in 2021 coincided with the launch of a specific crisis programme which provided a general guarantee of 80% at no cost for the initial 12 months, but was not purely driven by this new programme. Overall, crisis guarantees constituted 26% of all guarantees issued that year, the remainder being granted under the general programme to mature enterprises (39%), followed by women entrepreneurs (19%) and young entrepreneurs (9%). The crisis mechanism was extended in 2022 to counter the effects of the war in Ukraine. The sectors that benefitted the most from the programme were agriculture and wholesale and retail trade, which together make up nearly two-thirds of recipients. The remainder goes to industry, services and other sectors (ODA, 2021[30]). The fund is funded through fees, but also benefits from government budget transfers and funding from international financial institutions, such as the World Bank, which approved funding in June 2022 to support the launch of a portfolio guarantee mechanism (World Bank, 2022[31]).[11]

In June 2023, the government launched a new subsidised funding programme, "373", through which SMEs can access investment loans of up to MDL 15 million (EUR ~780 000) at an 3% interest rate for FX loans and 7% for local currency loans, with a grace period of up to 3 years. These interest rates are significantly cheaper[12] than current market rates and, depending on how strongly the programme takes hold, could lead to potential distortions in the lending environment. In parallel, businesses can benefit from a loan guarantee of up to 40% through the FGC. The motivation is to stimulate the economy and incentivise investment. The launch of this new programme moves Moldova into the territory of support mechanisms that are generally considered to be less sustainable as they constitute a greater drag on public finances than, for instance, guarantee programmes. The initial budget of MDL 255.7 million (EUR ~13.4 million) is quite substantial compared to the annual investment volume of the Credit Guarantee Fund of MDL 388 million (EUR ~20 million) in 2021. Given that the funds provided under the "373" programme are a straight transfer of government subsidies, it will need to be very carefully monitored to evaluate its effectiveness and ensure an efficient use of public resources for the policy objectives that have been set out.

When it comes to non-bank financing sources, microfinance is widely available in Moldova through non-bank credit organisations (NBCOs) and credit associations. The latest update of the Law for Non-bank Credit Organisations was in 2018, bringing various forms of alternative finance under one regulatory umbrella. Previously, the regulatory oversight for non-bank financing institutions was provided through the National Commission for Financial Markets, but regulation and supervision were transferred to the National Bank of Moldova on 1 July 2023 (according to Law No. 178/2020). NBCOs are prohibited from raising deposits and mainly fund themselves through banks and international non-bank financial institutions. Credit associations mainly fund themselves through bank loans, and in some cases, deposits. In addition, Law No. 01/2018 set limits for how much NBCOs can charge for consumer loans. The non-bank financing sector is about ten times smaller than the commercial banking sector, with total assets of

nearly MDL 14 billion (EUR ~730 million) as of Q3 2022, including financial leasing activities. However, the vast majority of loans go to individuals rather than businesses.

Leasing activities are set out in the Civil Code, Chapter X, last updated in 2019, which provides a reasonable legal framework. The majority of leasing agreements cover vehicles (91%), although it is possible to lease equipment as well. The Civil Code, Chapter XXIV, also sets out the legal framework for factoring, including definitions of different types of factoring. A small number of dedicated companies and banks provide factoring services in Moldova. National statistics are difficult to find, but FCI statistics suggest that factoring volumes in Moldova amounted to only EUR 3 million, by far the lowest penetration in the region (FCI, 2022[32]).

There is no dedicated legal framework for venture capital (VC), but provisions around VC have been introduced in existing legislation, governing, for instance, the activities of alternative organisations of collective investment (e.g. VC funds) or business angels. Certain restrictions exist on VC investments for institutional investors such as pension funds and insurance companies,[13] thus reducing the scope of available capital for these types of investments.

Venture capital remains at a nascent stage in Moldova, with no clear strategy or support mechanisms in place to catalyse the sector. A business angel association exists ("Business Angels Moldova") and brings together individuals who invest in start-ups, but its activities and outreach appear to be rather limited. Data on VC transactions are difficult to find, but anecdotal evidence suggests that activity is very modest, with significant room for development.

### *Financial literacy*

Moldova conducted financial literacy surveys among its population on a more continuous basis in 2018, 2020 and 2022. The latest survey also feeds into the formulation of a new financial literacy strategy , still under preparation. The survey aims at evaluating the financial literacy of the general population, however, without additional modules around entrepreneurship-related issues. Nevertheless, regular surveys are important means to take more informed policy decisions in this area. It should be noted that the financial literacy of entrepreneurs has been subject to a recent OECD survey conducted in a number of countries in Southeastern Europe (SEE) and the Caucasus in 2021 and 2022. The survey suggests that financial literacy among Moldovan entrepreneurs is low, both in comparison to countries in SEE and to G20 economies. This illustrates how important it is to target entrepreneurs and financial concepts specific to their realities specifically (OECD, 2023[33]).

In terms of implementation, financial literacy is part of the secondary school curriculum, but only as an elective. ODA provides certain trainings that include information around types of financing for SMEs, as well as digital finance issues. In the absence of a formal strategy, there is no monitoring and evaluation of financial literacy specific programmes, but the National Bank of Moldova and the National Commission for Financial Markets do report on their activities in the field.

### *Digital financial services*

There is currently no strategy or action plan for digital finance in Moldova, and no inter-ministerial hub or task force has been set up to look into issues related to digital financial service provision. A dedicated FinTech division was, however, created in the National Bank of Moldova in September 2022, which is an important step toward formulating good policies in this area, although a multi-disciplinary approach involving partners from other ministries and authorities should be considered. Activities are already taking place, with a lending marketplace already in existence, and the expectation of crowdfunding becoming an option once a new draft law on this matter has been passed.

The National Bank's approach to regulating digital financial services is activity-based and some provisions exist with regard to outsourcing arrangements and finance providers' operational resilience frameworks.

### *The way forward*

Going forward, Moldova should continue on its path of strengthening the regulatory and supervisory framework for its financial sector. This includes continuing the NBM's efforts to incorporate ESG reporting and climate-related stress testing into supervision frameworks to be better prepared for climate-related impacts on businesses which could knock on to bank operations.

The expansion of the Credit Guarantee Fund and the introduction of the "373" programme make the use of robust monitoring and evaluation systems even more pertinent. In addition to regular monitoring activities, specific evaluation efforts should be introduced to ensure that these instruments deliver policy objectives in the most efficient and effective way.

Non-bank financing mechanisms could be further improved through adjustments to existing legal and regulatory frameworks to remove any uncertainty that may still inhibit their uptake. In addition, efforts to raise awareness of alternative funding options can go a long way in making entrepreneurs more comfortable with instruments they are less familiar with, but that can constitute an important alternative to bank financing by being more accessible, cheaper or more tailored to SMEs' needs. The government should also consider ways to support the VC sector, for example, through the establishment of a fund of funds or activities that can broaden the investor base. In terms of digital finance, the government should adopt a multi-disciplinary approach to analysis and policy decision making that takes into account the complex nature of the issues involved.

Finally, it will be important to finalise, approve and implement the proposed financial literacy strategy. The strategy should incorporate considerations around financial skills for entrepreneurs, including content, and outreach.

## *Pillar D: Access to markets*

### *Public procurement*

The COVID-19 pandemic and the war in Ukraine, among other factors, have delayed the implementation and follow-up of the public procurement reforms envisaged at the time of the 2020 Small Business Act assessment. A number of challenges thus remain regarding public procurement and SME access to it.

There have only been minor changes to the legal framework since the last assessment. Public procurement remains regulated by the Public Procurement Law (PPL) of 2016 (Parliament of Moldova, 2015[34]), complemented by the Regulation on Low-Value Procurement of 2016 (Parliament of Moldova, 2016[35]). Procurement by utilities is covered by the Utilities Law of 2020 (Parliament of Moldova, 2020[36]). State-owned enterprises are required to apply a specific procurement regulation issued in 2020 (Parliament of Moldova, 2020[37]). The contract value thresholds for the applicability of the PPL were recently raised (in the case of goods and services, from MDL 200 000 to 300 000, or EUR ~10 400 to ~15 700) and a new regulation for procurement of goods below these new thresholds has been adopted (Parliament of Moldova, 2022[38]). However, these changes did not enter into force until 1 July 2023.

The institutional framework remains the same. The Ministry of Finance sets public procurement policies and the Public Procurement Agency (PPA) manages their application. Complaints against acts by contracting authorities (or their failure to act) are dealt with by the National Agency for the Resolution of Complaints, but only for contracts covered by the PPL or the Utilities Law. For low-value contracts, claimants have to go to the regular courts: a major disincentive for SMEs who believe they have been wronged.

The electronic infrastructure for public procurement (the MTender system, mtender.md) was updated in 2021 and 2022, adding functionalities for restricted tenders and framework agreements as well as for business intelligence, and adjusting it to the legal requirements for tender evaluation. With only a few

exceptions, it remains compulsory to use it only for procurement under the PPL. Consequently, MTender only contains records for such contracts; data on low-value contracts are not generated and thus not available in the system. However, low-value procurement, less regulated and monitored, is estimated to account for the same share of the total value of public procurement as contracts concluded using MTender.

The Public Procurement Strategy 2016-2020 was not followed by a new five-year strategy for the period 2021-2025. However, the upcoming preparation of a Public Procurement Development Programme for 2023-2026 was announced on 23 January 2023 (Ministry of Finance, 2023[27]) and a full draft has been prepared, aligned with the new Strategy for the Development of Public Financial Management 2023-2030, a draft of which was published in January 2023 (Government of Moldova, n.d.[39]).

These initiatives are intended to address the various shortcomings which negatively affect SME access to public procurement:

- Price remains the main award criterion, as lack of skills and capacity in contracting authorities means that criteria for quality, performance, life cycle costs, etc. are hardly used at all – to the detriment, for example, of innovative SMEs offering better-quality goods.
- Procurement opportunities for low-value contracts are seldom published, in practice making them accessible only for those SMEs and other enterprises which maintain personal contacts with decision makers.
- Small-value contract awards are not published in a timely and readily accessible manner, adding to the difficulty to lodge meaningful complaints against contracting authorities' decisions.
- Responsibility for observing the guiding principles for small-value procurement lies with the contracting authorities, but they lack skills, resources and incentives for doing so.
- Low-value procurement is not otherwise effectively monitored, supervised or reported on, allowing fraud and corruption to occur and be hidden.

Their effect has been to strongly reduce effective competition, creating strong disincentives for serious SMEs to participate in public procurement and leading to less value for money in the use of public funds, as well as inefficiencies in the work of contracting authorities.

Addressing these points requires taking on the following challenges as a continuation of current reform efforts. To this end, Moldova should i) update and complement MTender, including a full range of functions for using other award criteria than price and for low-value procurement, and raise user skills; ii) approve the public procurement development programme 2023-2026 and start to implement it, with added focus on SME access to public procurement; and iii) ensure the wide, comprehensive generation of public procurement data, making it readily available and using it to improve policies and procedures and ensure they are fully applied.

### *Standards and technical regulations*

Moldova has made significant progress in aligning technical regulations and quality infrastructure (QI) with the WTO and the EU since the last SME Policy Index assessment in 2020. In parallel, Moldova reported a significant increase in exports to the EU by 14% from 2021 to 2022 (from EUR 1.83 to EUR 2.56 billion) after small decreases in the previous two years (European Commission, 2023[40]).

A key accomplishment in terms of overall co-ordination and general measures was the amendment of Law No. 420/2006 on Technical Regulations in 2020, which brought Moldova's technical regulation in line with the provisions of the TBT-WTO Agreement. To improve its QI and strengthen institutional market surveillance capacities, Moldova established the State Inspectorate for the Supervision of Non-Food Products and Consumer Protection based on the re-organisation of the Agency for Consumer Protection and Market Surveillance. Likewise, the government launched the re-organisation of the National Institute of Metrology. Various additional technical regulations have been approved since the 2020 assessment.

Regarding harmonisation with the EU Acquis, Moldova could intensify its various collaborations with the EU. Approved in 2022 and entering into force in January 2023, the Institute for Standardisation of Moldova (ISM) became a CEN and CENELEC Affiliate. Likewise, MOLDAC received the recognition of the European Co-operation for Accreditation (EA), ensuring the acceptance of Moldova's accreditation of conformity assessment bodies in all EU Member States. In addition, Moldova adopted 100% of the EN standards as national standards.[14] An action item is the implementation of new standards by Moldova's companies. In response, ISM offers trainings and various additional support measures have been introduced (see also the next section). A remaining standards-related challenge is the permanent translation of new EU standards. Regarding the conformity assessment, most priority sectors have assessment bodies compliant with EU requirements. The adaptation of the certification landscape in the remaining priority sectors will be an important future action. The further development of evaluation practices is another important next step for Moldova's QI.

To improve SMEs' access to standardisation, Moldova supports the purchase of standards and their participation in the development of standards by various financial and non-financial measures. Specific accomplishments are two new state programmes for SMEs' Growth and Internationalisation and on SMEs' Greening. They entered into force in 2020 and promote the implementation of international standards and certification, for example via business vouchers and the SME Greening Program's grant of up to Leu 500,000 for the implementation of standards and international certificates relevant to greening, the introduction of the European ecological management and audit system, and the preparation for ecological labelling. Likewise, ISM organises training events to help stimulate the implementation of new standards. In the same way, ODA, in partnership with ISM, provides information sessions for entrepreneurs on the benefits of implementing international standards and the role of standards for internationalisation. In addition, it has an "Activity Strategy" for 2021-23 that is also focused on education projects and works on the establishment of a standardisation academy. A recommendation to maximise the impact of these initiatives is to also consider SME-specific issues in the education plan on standardisation in the next version of ISM's Activity Strategy and in the academy.

The digitalisation of standards and technical regulations has begun. ISM, for example, implemented SM EN ISO 22301 in response to the pandemic, also facilitating SME's remote participation in standardisation. The digitalisation of Moldova's QI and the authorities in charge of technical regulations as a whole will require significant additional efforts in the coming years, e.g. regarding the digitalisation of conformity assessment activities as well as the development and implementation of action plans for the digitalisation of metrology and market surveillance.

### *Internationalisation of SMEs*

Moldova has taken important steps forward to support SMEs' internationalisation since the previous SBA assessment, especially in the fields of export promotion and support to SME use of e-commerce.

The country stepped up efforts to promote exports among SMEs, significantly improving policies and programmes to support and facilitate their entry into international markets. Although the two cornerstone policy documents supporting SMEs' internationalisation (i.e. the National Strategy for Investment Attraction and Export Promotion for 2016-2020 and the Strategy for SMEs Sector Development for 2012-2020) expired in 2020, at the beginning of 2022, the government presented the draft PACC 2023-2027. According to the draft, one of the programme's specific objectives will be "strengthening SMEs' competitiveness and improving market access". This objective relies on several actions, such as organising matchmaking events to facilitate business-to-business contacts, implementing the SME Internationalisation Programme, and supporting SME clustering through the Support Programme for Clustering Initiatives as a way of integrating into global value chains (GVCs).

Nevertheless, there are currently several active programmes to promote SME internationalisation. These programmes are co-ordinated by two different agencies: ODA and Invest Moldova, the country's

investment promotion agency. Invest Moldova's mandate is rather broad, as it includes country brand promotion, supporting investment activity and protecting investments, export promotion, tourism promotion, and strengthening and implementing economic diplomacy. In terms of export promotion, the agency provides financial support through specific instruments. Its financial contribution comes from the state budget in the form of partial funding for activities related to organising participation in fairs, exhibitions and events; organising business forums and business-to-business meetings; and organising internal and external study visits (Invest Moldova, 2023[41]). In 2020, the government adopted the State Program for SMEs Growth and Internationalization (Government Decision No. 439/2020), aiming at strengthening SMEs' capacities to access international markets. The programme, co-ordinated by ODA, foresees financial support for SMEs allocated via two types of financial instruments. Business vouchers are offered for up to MDL 100 000 (EUR ~5 000), covering costs related to website creation, consultancy on intellectual property protection, the establishment of logistics process and the preparation of export documents, the promotion of products and services through national and international electronic platforms, market research, etc. In addition, grant schemes for up to MDL 2 million (EUR ~100 000) are available to SMEs to cover investments for the acquisition of tangible and intangible assets. The grant scheme follows the principle 1+1 (each MDL offered by the state should be complemented by MDL 1 from the SME's own resources). In 2022, 34 grants were approved, for a total financial support of about MDL 44.46 million (EUR ~2.3 million). Moldova's monitoring activities are also very advanced, with monitoring mechanisms in place for internationalisation programmes as well as ODA itself. In addition, the list of beneficiaries of financial support is made public on the agency's website.

Government Decision No. 614/2013 introduced the concept of clusters for the first time in Moldovan legislation, setting out the government's commitment to develop them, as well as relevant regulatory mechanisms. In its efforts to update and further expand cluster development, at the end of 2021, the Ministry of Economy developed and presented for public consultation the State Programme to facilitate the grouping of SMEs in clusters. According to the draft programme, it aims to catalyse cluster formation and SMEs integration into regional innovation ecosystems based on cluster co-operation. Moreover, the Ministry of Economy and ODA are in the process of developing the Local Supplier Programme to encourage the integration of local SMEs into GVCs. The programme will focus on building links between domestic manufacturing SMEs and international buyers, including multinational companies.[15] However, there are currently no active programmes specifically targeted at SME integration into GVCs, and all initiatives to enhance the participation and engagement of SMEs in global production networks fall under the State Programme for SMEs Growth and Internationalisation. One initiative worth mentioning is the BusinessLink platform (businesslink.md), the first national supplier database, which serves as a resource for foreign investors and international companies to explore local SMEs with high potential across different sectors (Box 13.3).

### Box 13.3. *BusinessLink*: the official suppliers' database and linkages platform in Moldova

In 2021, ODIMM developed the BusinessLink platform to assist entrepreneurs in identifying business partnerships. The platform includes centralised information about active and qualified domestic companies providing services and products both on the internal and external market. It serves three main functions: i) it provides access to the profiles of businesses willing to integrate into GVCs, ii) it collects and present RFQs of Moldovan and international buyer companies in a section (RFQ Connect) devoted to calls for tender requested by interested companies, and iii) it offers a calendar that allows users to create and track B2B matchmaking events.

The platform was implemented by the Agency for International Cooperation of Germany (GIZ) Moldova with the financial support of the Federal Ministry for Economic Cooperation and Development of Germany and the Swiss Agency for Development and Cooperation (SDC).

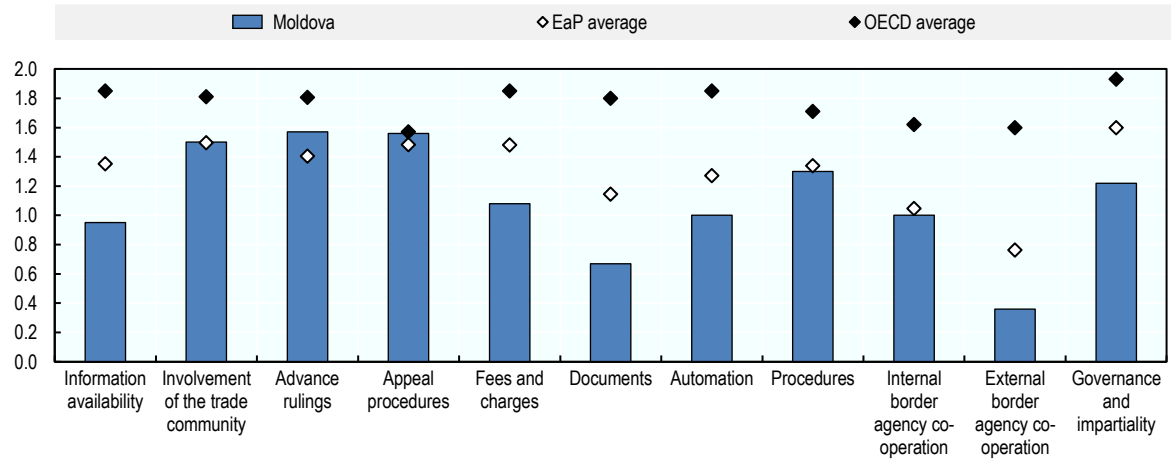
In 2022, two experts were trained to provide support to SMEs in the creation of their profile and the registration on the BusinessLink platform, as well as on how to use all the available functions and services. The platform was promoted and publicised at different events, such as business forums and expos, and, with the support of GIZ, a promotion campaign was carried out.

Source: (BusinessLink, 2023[42]), (ODA, 2021[43]), (moldpres, 2021[44]).

Moldova has made significant strides in the use of e-commerce for hybrid retail among SMEs since the last SBA Assessment. The government's vision on e-commerce and hybrid retail is encompassed in the draft Digital Transformation Strategy (DTS) of the Republic of Moldova for 2023-2030, published for public consultation in December 2022. One of the strategy's main objectives is "creating an innovative and resilient digital economy". Among the key actions identified to achieve this objective are the development of e-commerce to stimulate economic growth and development, improving e-commerce and e-payments, and strengthening and attracting national and international e-commerce platforms in the country. However, until the strategy is adopted, e-commerce support is being expedited through the SMEs Digital Transformation Programme, adopted by the government in 2022 (Governmental Decision No.129/2022). The programme aims at supporting SMEs to integrate digital technologies into their operations by offering non-refundable financial support up to MDL 500 000 (EUR ~26 000) for SMEs, including to cover expenses related to the procurement of IT services and solutions for e-commerce. Finally, it is important to mention the adoption of Law no. 60/2023 on the amendment of some normative acts (referred to as "Legislative Package for the Stimulation of Electronic Commerce") was recently adopted. This legislative package provides for the updating of the regulatory framework on internal trade and its completion with the necessary additional provisions on electronic commerce; adjustment of the normative framework regarding information society services, with the extension of the scope including non-resident service providers that direct their activity to Moldova; consumer protection in the electronic commerce process; and other related provisions (United Nations, 2023[45]).

With regards to trade facilitation, the effectiveness and efficiency of Moldova's trade facilitation measures could be significantly improved (Figure 13.5). Although the country outperforms the EaP average in the OECD Trade Facilitation Indicators with regard to advanced ruling and appeal procedures, Moldova should direct efforts towards reducing the interval between the publication of trade-related regulations and their entry into force, as well as improving the availability of online, comprehensive information on applicable fees and charges and reducing the number and diversity of such fees and charges. Moreover, the country should expand the acceptance of copies of documents, reduce their number and the time necessary to prepare them and simplify trade-related procedures.

## Figure 13.5. OECD Trade Facilitation indicators for Moldova (2022)




Note: Trade facilitation indicators take values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade Facilitation Indicators Database, https://oe.cd/tfi.

StatLink https://stat.link/qbv8lw

In this context, it is also important to mention that Moldova is the only country in the EaP region that is a member of the Central European Free Trade Agreement (CEFTA). The objective of the Agreement is to harmonise its parties' regulatory framework with the EU and international standards to enhance trade in goods and services, eliminate trade barriers, and attract investments through fair, stable and predictable trade rules.

To conclude, moving forward, Moldova should capitalise on the momentum and ensure the swift adoption and implementation of the draft policy documents related to supporting SMEs' internationalisation, including the PACC, the State Programme to facilitate the grouping of SMEs in Clusters, the Support Program for Clustering Initiatives, and the Digital Transformation Strategy. ODA's transparency could be improved by ensuring an independent assessment of its activities in relation to SME internationalisation support.

### *Pillar E: Innovation and business support*

#### *Support services for SMEs and start-ups*

The Programme for Promoting Entrepreneurship and Increasing Competitiveness 2023-2027 (PACC) is the foundation of Moldova's provision of business support services for SMEs and start-ups. Improving entrepreneurial culture and the capabilities of Moldovan SMEs is one of its five strategic objectives. Its first action plan is expected to be approved in the second half of 2023, although the estimated costs for many of its activities are still unspecified, which may pose a challenge for implementing institutions' forward planning.

ODA is the main government agency with a strong mandate to support Moldovan SMEs through a wide range of financial instruments, mostly funded by donors. ODA is the main government agency with a strong mandate to support Moldovan SMEs through a wide range of financial instruments, co-funded by international donors. In addition to managing a Credit Guarantee Fund (see above), ODA offers grants to women entrepreneurs (up to EUR ~9 000), start-ups led by young entrepreneurs (up to EUR ~10 000), and fast-growing SMEs willing to upgrade their production capacity and internationalise (up to EUR ~110 000). The flagship programme PARE 1+1 (MDL 1 invested matched by a grant of the same amount), which

aims to incentivise the investment of remittances in starting or developing a business, has been updated with a “1+2” component for those entrepreneurs who successfully implemented the “1+1” project. All financial support programmes have a strong co-financing component to be provided by the beneficiaries, which increases in share with the absolute size of the grant.

Specifically to support the digital transformation of SMEs, in 2022, ODA introduced a dedicated programme structured around three pillars: i) raising awareness of the opportunities of increased digitalisation; ii) financial support in the form of grants (up to MDL 500 000 / EUR ~26 000) for the purchase of a wide range of digital solutions (both hardware and software), as well as consulting and training services to build internal capabilities for the digital transformation; and iii) individual mentoring on the implementation of digital transformation plans.

On the non-financial side, ODA manages a network of 11 business incubators and has re-organised its training offers around three main pillars, which are clearly advertised on the agency’s website and respond to the needs of the different segments of the SME population: 1) “Start in Business” for start-up entrepreneurs willing to develop a viable business plan around their ideas; 2) “Efficient business management”, covering a wide range of business management topics for SME managers (e.g. financial management, marketing and sales, human resources); and 3) “Business expansion and internationalisation”, targeting SME managers with an ambition to develop their business internationally.

As a welcome development, the government has placed a greater emphasis on facilitating SMEs’ access to external providers of business support services. While ODA has strengthened its role as a one-stop shop, co-ordinating and, in some cases, directly delivering services to Moldovan SMEs, all grants available to SMEs can be used to procure advisory services from the external consultant of their choice. This makes specific industry or business expertise more affordable to SMEs, while helping to develop the local supply of consulting services in Moldova.

Lastly, some improvements should be mentioned on the government’s practices to monitor the delivery of SME support services, with rigorous tracking of the number of beneficiaries and amounts disbursed as presented in the informative report on the implementation of the SME Strategy 2012-2020 (e.g. on average, each year: 176 projects financed under the PARE1+1 project, over 8 200 people consulted and MDL 117 million/EUR ~6 million guaranteed loans). However, evaluation mechanisms to assess the impact on the business performance and capture economic additionality of the various support programmes are not a regular practice, even though ODA recently conducted an initial impact assessment for its programmes implemented in the period 2011-2021 and aims to further improve this area with capture beneficiaries’ satisfaction through dedicated feedback mechanisms.

Moving forward, the government could build on current efforts to ease SME access to external advisors and incorporate quality assurance mechanisms for certified consultants. Further, more rigorous impact evaluation efforts could be made to complement the current practices of monitoring SMEs’ take up of support programmes.

### *Innovation policy for SMEs*

The National Program in the Field of Research and Innovation 2020-2023 (NPRI) is the current strategic document guiding innovation policy in Moldova. It embraces the principles of smart specialisation[16] and has identified energy, ICT, agriculture and biosciences as preliminary areas of specialisation. While not explicitly referring to SMEs, the NPRI’s action plan does include a set of measures relevant for Moldovan start-ups and SMEs, in particular to promote science-industry collaboration, the creation of spin-offs from research institutes, and science and technology park-based innovation. In these areas, the NPRI connects well with the PACC (see previous section), although the costs and allocated funding for many of the activities in its action plan are still unspecified.

The National Agency for Research and Development (NARD) and ODA are the main institutional bodies with a mandate to support innovation in Moldova, with a leading role to implement SME-related measures in the NPRI. NARD, in particular, monitors the activity of a network of science and technology parks and innovation incubators matching the specialisations of existing scientific-technological clusters. In addition, the national ecosystem for supporting innovation among SMEs is complemented by interesting non-governmental initiatives, such as the Moldovan Technology Transfer Network and Tekwill. The Moldovan Technology Transfer Network is a non-profit organisation striving to increase human and material resources for scientific teams and facilitating SMEs' access to technological services and scientific infrastructure. Tekwill, on the other hand, supports the acceleration of new products and tech start-ups through financing opportunities, mentoring and consulting sessions with industry experts, and access to an extensive business network.

Financial support for innovation in Moldova remains rather limited, although new instruments have been introduced since the previous SBA assessment. NARD continues to implement its "Innovation and Technology Transfer Project", which provides funding (for a maximum of 50% of total project value, or MDL 1 million / EUR ~50 000) on a competitive basis for collaborative projects between research organisations and businesses aimed at developing new or improved processes, products, services, or technologies. ODA, on the other hand, has introduced a new "Programme to Support Digital Innovations and Technological Start-ups", awarding grants to stimulate research and development; prototyping; and innovation in the field of information technologies and communications, industrial production, and green technologies.

Overall, financial support for innovative SMEs does not seem adequate for achieving the NPRI's objectives, with NARD's and ODA's budgets for the programmes described above being around EUR 275 000 (12 projects financed in 2020) and EUR 300 000 (14 SMEs financed as a result of applications received in 2022), respectively. Indirect types of financial incentives for R&D and innovation are also lacking.

Some information on innovation performance in Moldova is available. Every two years, the National Bureau of Statistics produces indicators on the number of SMEs introducing product or process innovations, which is a valuable first step towards building a more complete set of outcome-oriented indicators. In addition, monitoring and evaluation of innovation support could be expanded to cover individual programmes, since the current assessments of the initiatives promoting co-operation between innovative SMEs and universities/research centres do not analyse the specific impact on SMEs' innovation performance.

Moving forward, the government could consider introducing indirect (market-based) incentives for R&D and investment in innovation (such as accelerated depreciation for investment in technological equipment and tax credits for expenditures on highly skilled labour), increasing SME awareness of available support programmes to expand the number of applications received, and gradual incorporating an evaluation of the impact of support programmes into its regular monitoring of innovation policies.

### *SMEs in a green economy*

Moldova has made considerable efforts to diversify its energy sources and increase the security of both electricity and gas supply. Further integration with Europe for both gas and electricity imports is ongoing as Moldova prioritises moving away from Russian sources of energy. The March 2022 emergency synchronisation with ENTSO-E, [17] triggered by of the war in Ukraine, has pushed Moldova closer to full electricity trade with Europe, which also opens up additional opportunities to increase the share of renewable energy in total energy supply for the country (IEA, 2022[46]). SMEs can play a role in this energy transition by also seeking to become more resource efficient as a way to improve production while minimising pollution and the generation of waste. For SMEs, even the smallest resource efficiency and cleaner-production measures can yield important results (EU4Environment, 2023[47]).

The policy framework for greening SMEs in Moldova has evolved considerably since the previous SBA assessment, with two important policy documents shaping the environmental approach targeting SMEs

adopted in 2022: 1) the National Development Strategy "European Moldova 2030", which clearly stipulates the greening of SMEs, creating green jobs, promoting eco-innovations and eco-labelling for products and services offered by SMEs as priorities; 2) the "Law on Industrial Emissions", which establishes a regulatory framework for industrial pollution, promotes the application of best available techniques and introduces integrated environmental permitting. These are complemented by the more operational "National Program on Greening of SMEs", adopted in 2019 in the context of the EU4Environment project, and providing a range of support measures (see below). The Ministry of Environment is the main body in charge of developing and monitoring environmental policies for SMEs, while ODA has strengthened its role in promoting greening practices directly to entrepreneurs.

Moldova continues to disincentivise the use of natural resources and limit pollution, and has introduced regulatory and financial incentives to help expedite the greening of SMEs. On the one hand, the Law on "Payments for Environmental Pollution" established tax measures related to the use of natural resources (e.g. water, minerals, standing timber) and charges for environmental pollution. On the other hand, financial incentives have recently been introduced through the Greening Program for SMEs and the Energy Efficiency Program for SMEs, both implemented by ODA.

Through these programmes, SMEs benefit from information materials, consultancy support and training services to identify solutions and take concrete actions to green their production processes. Interestingly, an online self-assessment tool is available to help enterprises assess their environmental performance and prioritise areas for improvement. These measures are complemented with dedicated financial support instruments: the Greening Program for SMEs offers grants up to MDL 500 000 (EUR ~25 000) to be used on expenditures related to resource efficiency, the application of sustainable production models, the introduction of eco-innovations, waste reduction and management, pollution prevention, and water resources management. The Energy Efficiency Program for SMEs foresees allocations of matching grants up to MDL 1 500 000 (EUR ~ 75 000) for investment in machinery and equipment using alternative energy sources. Although these initiatives are a very welcome development in Moldova, evidence on the implementation of a separate Programme on the Promotion of Green Economy for the period 2018-2020 has been slow, with only around 50-60% of the activities in its action plan reported as implemented.

On monitoring and evaluation, the lack of relevant statistical data remains a considerable challenge in conducting a comprehensive evaluation of environmental policies targeting SMEs. Although implementing agencies track the number of SMEs that have benefited from public financial support to reduce their environmental footprint, there are no available data on the number of SMEs with ecological/green certificates, using environmental management systems, having implemented pollution reduction measures, or offering green products or services.

Moving forward, Moldova could consider further reforming its environmental regulatory framework, embedding a stronger focus on promoting greening by SMEs; supporting SMEs in identifying greening projects which could become eligible for financial support; and improving the production of nationwide statistical information on the environmental and greening performance of SMEs.

## The way forward

Since the previous SBA Assessment, Moldova has witnessed consistent progress in fostering SME development, including their digital transformation, through diverse initiatives. To complement its current approach, the government should contemplate the following measures:

- While Moldova has made significant strides in policy design, the previous *Digital Moldova 2020* Strategy had achieved only 50% of its objectives due to factors such as insufficient co-ordination and institutional capacity, funding, and monitoring. Moldova will therefore need to ensure the new National Digital Strategy is fully implemented, clearly defining stakeholders' roles and ensuring

adequate funding, as well as rigorous monitoring and evaluation process, incorporating pertinent indicators to measure advancement towards the set objectives. Moldova should continue its efforts to narrow persisting digital disparities, notably by enhancing the affordability of fixed broadband to meet the ITU's 2% target and fostering broadband uptake among small businesses. Comprehensive size-disaggregated data collection would be needed to evaluate disparities in terms of connection quantity and speed among firms of varying sizes. Additionally, fostering inclusive broadband policies calls for expanded multi-stakeholder consultations, encompassing network operators, consumers, regulatory bodies, and all levels of government. To enhance its digital skills strategies, Moldova should strengthen its multi-stakeholder approach, notably involving the Ministry of Labour and Social Protection, ANOFM, employers, and teachers for co-ordinated digital skills assessment aligned with labour market policies. Forming a National Digital Skills and Jobs coalition in line with EU4digital guidelines could facilitate this. Lastly, Moldova should further promote digital skills development for businesses, particularly smaller enterprises, adopt a comprehensive digital competence framework, and refine skills assessment practices through data collection, policy monitoring, and potential expansion of skills anticipation exercises. In terms of strengthening the institutional framework in Moldova for SMEs, it is imperative to finalise the transformation of ODA, aligning its resources and functions seamlessly with the objectives outlined in the new SME Development Strategy. Expediting regulatory reforms is paramount to meet impending EU accession prerequisites and harmonise SME policy guidelines with EU standards, including the comprehensive evaluation within the SBA annual performance review. A proactive approach is necessary to gauge the efficacy of enterprise support programmes and the operational efficiency of public agencies. This gains particular significance considering the potential elevation of EU technical assistance funding linked to the accession trajectory. Furthermore, the strategic implementation of an SME-focused RIA test is instrumental. In tandem, expanding e-platform accessible services, boosting SME involvement in e-government services, establishing a streamlined online tax information portal managed by the Tax Administration, and systematically assessing the impact of varied tax rates and incentives on enterprise growth warrant diligent attention. Further strengthening the framework involves conducting exhaustive surveys and consultations with representatives from the SME sector to refine the intricacies of the SME tax regime. To tackle the challenges related to insolvency and early identification of financial distress, Moldova's focus must centre on expediting the approval and implementation of the Second Chance Program, and concurrently enhancing the monitoring and evaluation mechanisms concerning bankruptcy-related programmes and regulations. This strategic approach will ensure a comprehensive assessment of effectiveness across all dimensions.

- In terms of entrepreneurial learning, Moldova could strengthen its approach by ensuring monitoring and evaluation of upcoming key strategies like Education 2030 and PACC, and all activities related to entrepreneurial learning in general. This approach aims to promote evidence-based policymaking and ensure the effective acquisition of entrepreneurial skills. The upcoming documents should also clearly define stakeholder responsibilities to facilitate co-ordinated implementation and maximise policy efficiency. Furthermore, Moldova can build upon successful instances of collaboration between SMEs and VET/ higher education institutions to further develop and strengthen these partnerships with general schools. As for women’s entrepreneurship, there is a need for concentrated efforts to support female micro entrepreneurs in rural areas, complemented by incentives to decrease women's participation in the informal economy. Expanding support for women entrepreneurs beyond the initial stages will contribute to project sustainability and business expansion. Improving data collection on women entrepreneurs, and their businesses, as well as conducting regular surveys addressing barriers for women entrepreneurs would be highly beneficial to inform policies through data insights. With regard to SME skills, Moldova could build on its ongoing efforts by improving its data collection, impact evaluation, and skills assessment and anticipation practices, which remain at a nascent stage.

Additional steps could include awareness-raising of training available, certification of competences, and encouraging peer learning and on-the-job training. Additionally, the smart specialisation approach should be enhanced by offering targeted training to SMEs in priority sectors and involving the Ministry of Labour and Social Protection and ANOFM, given their role in labour market policies.

- Moldova should continue strengthening the regulatory and supervisory framework within its financial sector, including by integrating ESG reporting and climate-related stress testing. Emphasis should be placed on implementing robust monitoring and evaluation systems for existing programmes and funds. In addition, to expand non-bank financing, Moldova should adjust to existing legal and regulatory frameworks to remove uncertainties and direct efforts towards raising awareness of alternative funding options. The country should also bolster the VC sector, for example by establishing a fund of funds. Finally, Moldova should adopt a multi-disciplinary approach to analysis and policy decision-making on digital finance, and finalise, approve and implement the proposed financial literacy strategy.
- To tackle the challenges of limited competition and SME disengagement in public procurement, which in turn undermines the value of public funds, the Moldovan government should fully align MTender with the PPL, incorporating robust functions for small-value procurement. It also involves launching the 2023-2026 public procurement development programme, with a focus on bolstering SME access. Additionally, comprehensive public procurement data should be generated and made easily accessible to enhance policies and ensure their complete implementation. Moldova has made significant strides in aligning technical regulations and quality infrastructure with WTO and EU standards since the SMEPI 2020 assessment. Despite these successes, there is room for growth in the evaluation of technical regulations, including frequency specifications in relevant laws. To bolster SME access to standardisation, Moldova offers support through state programmes and training events, with the recommendation to tailor these efforts to SME needs. Digitalization of standards, exemplified by ISM's implementation of SM EN ISO 22301 for Business Continuity Management, presents a promising avenue for progress, requiring substantial efforts in the coming years. On SME internationalisation, Moldova should leverage its current momentum by promptly adopting and executing the proposed policy measures. These include the PACC, the State Programme for SME Clustering, the Support Program for Clustering Initiatives, and the Digital Transformation Strategy. Moldova should also consider improving ODA's transparency by introducing an independent evaluation of its initiatives aimed at supporting SME internationalisation.
- In progressing ahead, the Moldovan government could enhance SME access to external advisors and ensure the quality of certified consultants. A more robust impact assessment approach could complement the existing monitoring of SME support programme uptake. In terms of innovation policy for SMEs, Moldova should explore the introduction of market-based incentives for R&D and innovation investment, along with integrating impact evaluation into routine monitoring of innovation policies. Furthermore, the Moldova government can take further steps to improve its environmental regulatory framework, giving prominence to initiatives that promote sustainability among SMEs. This could entail guiding SMEs in the identification of greening projects that qualify for financial assistance and enhancing the comprehensive gathering of nationwide statistical data concerning SMEs' environmental achievements.

## Table 13.5. Roadmap for policy reforms – Moldova

| |
|---|
| **Strengthening selected framework conditions for the digital transformation** |
| • Ensure implementation of the new National Digital Strategy, enhancing co-ordination across stakeholders, allocating necessary funds, and assigning clear roles. |
| • Establish effective monitoring and evaluation mechanisms with relevant indicators to track progress and impact. |
| • Address digital divides by improving fixed broadband affordability and uptake. |
| • Foster businesses' broadband adoption and gather data on digital divides among firms of varying sizes. |
| • Enhance broadband policy development through consistent multi-stakeholder consultations. |
| • Strengthen the multi-stakeholder approach for digital skills policies by involving relevant ministries, ANOFM, employers, and teachers, and consider establishing a National Digital Skills and Jobs coalition to this end. |
| • Further promote digital skills development among smaller businesses to bridge the digital transformation gap. |
| • Implement a digital competence framework, in line with EU's DigComp, to serve as a common basis and help certify the skills acquired. |
| • Enhance digital skills assessment and anticipation through data collection, monitoring & evaluation, and additional skills anticipation exercises. |
| **Enhancing the institutional and regulatory framework and operational environment for SMEs** |
| • Finalise ODA reform, aligning resources and structure with new SME Development Strategy goals. |
| • Accelerate regulatory reform for upcoming EU accession, align SME policy with EU standards (e.g. SBA performance review). |
| • Evaluate enterprise support programme efficiency and public agency performance to prepare for potential EU technical assistance funding increase during accession. |
| • Implement an SME-focused RIA test. |
| • Track SME engagement on Public Procurement electronic platforms, enhance participation in public consultations. |
| • Expand e-platform public services. |
| • Boost SME e-government usage through skill enhancement and promotions. |
| • Analyse diverse enterprise tax rates, regime effects, and growth outcomes. |
| • Survey SMEs and consult sector reps to refine tax policy and reduce non-compliance. |
| • Prioritise approval and execution of the Second Chance Programme. |
| • Strengthen monitoring and evaluation of current bankruptcy and second chance initiatives. |
| **Promoting entrepreneurial skills and women's entrepreneurship development** |
| • Ensure effective monitoring and evaluation of upcoming strategies (Education 2030 and PACC) and entrepreneurial learning initiatives to ensure evidence-based policymaking and skills acquisition. |
| • Define clear responsibilities among stakeholders to enhance co-ordination, implementation, and policy efficiency. |
| • Foster collaboration between general schools and SMEs to bolster entrepreneurial learning. |
| • Step up support for women entrepreneurs by expanding measures in rural areas, incentivising formalisation, and assisting women entrepreneurs beyond the initial stages. |
| • Improve data collection on women's entrepreneurship and consider conducting regular surveys to identify remaining barriers. |
| • Enhance skills assessment and anticipation by collecting data on SME skills, needs, and in-house training, sharing results on an online database. |
| • Develop improved skills anticipation tools, considering longer-term projections and a wider representation of businesses. |
| • Evaluate the impact of training on SME performance and encourage digital skills development, certification, and peer learning. |
| • Design targeted training for SMEs in priority areas of smart specialisation, involving relevant stakeholders for effective implementation. |
| **Facilitating SME access to finance** |
| • Integrate ESG reporting and climate-related stress testing into the legal framework for secured transactions. |
| • Establish robust monitoring and evaluation systems of existing programmes and funds. |
| • Enhance non-bank financing by addressing legal uncertainties and raising awareness of alternative funding options. |
| • Support the VC sector, possibly by establishing a fund of funds. |
| • Adopt a multidisciplinary approach to digital finance analysis and policymaking. |
| • Finalise, approve, and execute the financial literacy strategy, ensuring inclusion of entrepreneurial financial skills and outreach considerations. |
| **Supporting SME access to markets** |
| • Update MTender and raise user skills to better align with regulatory requirements and options, especially for using other award criteria than price and for small-value procurement. |
| • Complete the implementation of the 2023-2026 public procurement development programme with an added emphasis on enhancing SME access to public procurement. |
| • Facilitate the comprehensive generation and collection of public procurement data, ensuring its accessibility, and leveraging it to refine policies and procedures for full compliance. |
| • Continue the development of technical regulations' evaluation, considering specifying evaluation frequency in relevant laws. |

- Providing further priority sectors with conformity assessment bodies compliant to EU requirements.
- Integrate SME-specific considerations into education plans and initiatives for standardisation.
- Further digitalise standards and technical regulations, leveraging successful initiatives for broader adoption.
- Focus on digitalisation efforts for quality infrastructure and regulatory authorities to meet future challenges effectively.
- Prompt adoption and efficient implementation of draft policy documents such as the PACC, State Programme for SME Clustering, Support Program for Clustering Initiatives, and Digital Transformation Strategy.
- Enhancing transparency of ODA's activities in SME internationalisation support by incorporating independent assessments.

**Fostering innovation and business support**

- Expand efforts to enhance SME access to external advisors and ensure quality assurance for certified consultants.
- Strengthen impact evaluation practices to complement existing monitoring of SME support programme uptake.
- Explore the introduction of indirect incentives for R&D and innovation investment, along with continuous evaluation of support programme impact.
- Further reform the environmental regulatory framework to encourage green practices among SMEs.
- Support SMEs in identifying and pursuing greening projects eligible for financial assistance.
- Enhance the collection of nationwide statistical data on SMEs' environmental and greening performance.

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## Notes

[1] For more information on the analytical framework, please refer to the thematic chapter Digital Economy for SMEs.

[2] This number, however, reached 40% by March 2023.

[3] For more information and details on how Moldova could further promote digital business skills development, please see the OECD publication *Promoting digital business skills in the Republic of Moldova* (2023).

[4] It is also worth mentioning that the Moldovan government approved the Deregulation Package (Law 112 of 11 May 2023) to reduce bureaucratic barriers and requirements for business. The proposed legislative amendments concern a number of important areas of economic agents and are aimed at reducing business costs, reducing bureaucracy and improving relations between employers and employees.

[5] Conventionally called “Act for the digitization of the economy”.

[6] In this context, it is important to mention that the initiative “Remote Business Development in the Republic of Moldova/Contactless Business in Moldova” was approved on 26 May 2023. The initiative has the objective of analysing the online availability of essential public services for entrepreneurs and filling the legislative gaps to ensure the possibility to create and manage a company remotely in the Republic of Moldova.

[7] The “digital by default” principle provides that the Government should ensure the availability of at least one electronic method for requesting and obtaining the result of a public service. The “digital-first” principle prioritises documents in electronic format. While prioritising public services in electronic form, the principle of providing public services through multiple channels should be ensured; this implies that both physical and via electronic methods should be active. Relying on these principles, public institutions will be obliged to receive electronic documents and give priority to issuing documents in electronic format.

[8] This excludes certain types of income (e.g. subsidies, dividends, exchange rate differences, sources of income considered as non-taxable under the general tax regime).

[9] The Programme notably entails financial incentives and regulatory framework for infant nurseries, financial incentives for women that decide to return to work within twelve months of a child's birth, and incentives for paternal leave.

[10] For more information and detail on how Moldova could further promote digital business skills development, please see the dedicated OECD publication (2023), *Promoting digital business skills in the Republic of Moldova.*

[11] This is part of wider efforts to improve the attractiveness of credit guarantees, including amendments to the functioning of the existing programme set out in government decision no. 709 (19 October 2022).

[12] As of June 2023, the average interest rate on new business loans was 12.05% in local currency and 6.33% in foreign currency. (National Bank of Moldova, 2023[48])

[13] See, for instance, Law No. 198/2020 on private pension funds, and Law No. 92/2022 on insurance or reinsurance business.

[14] Several construction standards without national annexes.

[15] It is envisaged to include activities such as: developing a database on the capacity of local enterprises/documentation of SME capabilities; providing support for SMEs to create profiles on www.businesslink.md, as well as on other international portals; field visits to multinational companies; organising matchmaking events; etc.

[16] A place-based approach characterised by the identification of strategic areas for intervention based both on the analysis of the strengths and potential of the economy and on an entrepreneurial discovery process with wide stakeholder involvement. https://s3platform.jrc.ec.europa.eu/what-we-do

[17] The European Network of Transmission System Operators for electricity.

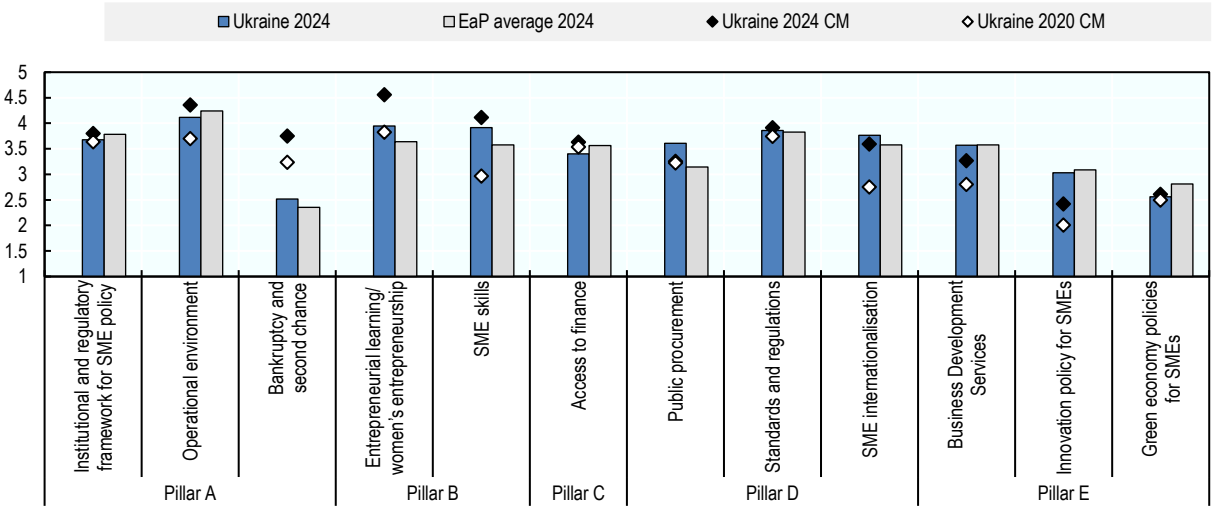
# 14 Ukraine: Small Business Act country profile

This chapter provides an assessment of the progress made by Ukraine in implementing the Small Business Act (SBA) for Europe over the period 2020-23. It starts with an overview of Ukraine's economic context and dives further into the characteristics of the country's SME sector. It then develops on the state of selected framework conditions for the digital transformation of SMEs. Finally, it analyses Ukraine's progress along twelve measurable dimensions grouped in five thematic pillars and sets out targeted policy recommendations.

## Key findings

### Figure 14.1. SME Policy Index scores for Ukraine

Country scores by dimension, 2024 and 2020 vs 2024 CM




Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

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### Table 14.1. SME Policy Index scores for Ukraine

Country scores by dimension, 2024 and 2020 vs 2024 CM

| Pillar | Dimension | Ukraine 2024 | EaP average 2024 | *Ukraine 2024 (CM)* | *Ukraine 2020 (CM)* |
|---|---|---|---|---|---|
| Pillar A | Institutional and regulatory framework for SME policy | 3.68 | 3.78 | 3.80 | 3.64 |
| | Operational environment | 4.11 | 4.24 | 4.36 | 3.70 |
| | Bankruptcy and second chance | 2.52 | 2.35 | 3.75 | 3.24 |
| Pillar B | Entrepreneurial learning/ women's entrepreneurship | 3.95 | 3.64 | 4.56 | 3.83 |
| | SME skills | 3.91 | 3.57 | 4.12 | 2.97 |
| Pillar C | Access to finance | 3.40 | 3.56 | 3.63 | 3.54 |
| Pillar D | Public procurement | 3.61 | 3.15 | 3.25 | 3.22 |
| | Standards and regulations | 3.86 | 3.83 | 3.91 | 3.75 |
| | SME internationalisation | 3.77 | 3.58 | 3.60 | 2.75 |
| Pillar E | Business development services | 3.57 | 3.57 | 3.27 | 2.80 |
| | Innovation policy for SMEs | 3.03 | 3.09 | 2.42 | 2.01 |
| | Green economy policies for SMEs | 2.56 | 2.81 | 2.61 | 2.49 |

Note: CM stands for comparable methodology. See the "Policy framework, structure of the report and assessment process" chapter and Annex A for information on the assessment methodology.

## Table 14.2. Implementation progress on SME Policy Index 2020 policy reforms – Ukraine

| Priority reforms outlined in the SME Policy Index 2020 | Key reforms implemented to date |
|---|---|
| **Pillar A – Responsive Government** | |
| Develop a new SME strategy and ensure there are sufficient resources to implement it.<br>Evaluate the effectiveness of the SME Development Office (SMEDO) and its position in the institutional framework.<br>Ensure that the new regulatory impact assessment (RIA) methodology is applied at all levels of government.<br>Expand the regulatory reform process, focusing on areas of low performance.<br>Implement an early warning system for detecting insolvency.<br>Adopt a second chance strategy for bankrupt entrepreneurs. | Transformation of the Export Promotion Office (EPO) into the Entrepreneurship and Export Promotion Office (EEPO) in 2021.<br>Regular review by the State Regulatory Service of Ukraine of draft regulations and their RIAs.<br>Launch of the Diia web portal, which offers e-services that simplify regulatory procedures for SMEs as well as information for entrepreneurs in financial distress. |
| **Pillar B – Entrepreneurial Human Capital** | |
| Consolidate the current monitoring and evaluation (M&E) actions and create an M&E framework for key competence development.<br>Develop a systematic approach to gathering SME skills intelligence data on a regular basis.<br>Implement a policy framework for women's entrepreneurship and develop a plan for activities in this sense.<br>Ensure gender-sensitive data collection on business activities. | Goals set in National Economic Strategy (NES) 2030 to develop entrepreneurial skills.<br>Additional steps taken to foster assessment of learning outcomes.<br>A wide range of training for women entrepreneurs, promoted on the Diia online one-stop shop.<br>Regular surveys on barriers to women's entrepreneurship.<br>Enhanced public and private training opportunities for SMEs.<br>The EEPO collects statistics and feedback on training. |
| **Pillar C – Access to Finance** | |
| Complete reforms to strengthen the legal framework for non-bank financing instruments.<br>Review SME financing support tools and ensure appropriate mechanisms are included to evaluate programmes. | The National Bank of Ukraine (NBU) allowed banks to use cloud storage abroad.<br>Support for SMEs through the government's 5-7-9 programme.<br>Update to the regulation on microfinance in 2021.<br>Launch of Diia.Business, which offers a range of knowledge and training on financial literacy, accounting, etc.<br>Adoption of a new Strategy for the Development of the Financial Sector of Ukraine in 2023, superseding the Fintech Development Strategy until 2025 approved in 2020. |
| **Pillar D – Access to Markets** | |
| Ensure the funding and capacity of the EPO to expand its support services.<br>Ensure the transparency and accountability of the trade financing programme provided through the Export Credit Agency (ECA).<br>Introduce measures to support SMEs' use of EU standards and conformity assessment services.<br>Improve the effectiveness of market surveillance.<br>Strengthen the review of public procurement activities, with a focus on the proper application of reasonable award and selection criteria.<br>Conduct capacity-building activities to raise the knowledge and skills of contracting authorities. | Development of a draft new Export Strategy, on the basis of information gathered through a business survey.<br>54 new EU-focussed technical regulations.<br>Order No. 285 of Ukraine's National Standardization Body "On the package adoption of the CEN-CENELEC European regulatory documents by Ukraine" to adopt 20 268 European CEN/CENELEC normative documents as national normative documents by 31 December, 2023.<br>Support and training on standards and technical regulations for SMEs, with a focus on integration into the EU Digital Single Market.<br>Development of a strategy for market surveillance.<br>Advice and support received from EU for further developing public procurement; PPL successively amended; procedures simplified and competition enhanced; new medium-term development programme drafted. |
| **Pillar E – Innovation and Business Support** | |
| Monitor the impact of innovation grants for SMEs and phase-in additional tools.<br>Introduce incentives to commercialise publicly funded research.<br>Establish a single information portal on starting/developing a business.<br>Improve M&E of support programmes to measure the impact on SME performance and assess the effectiveness of support infrastructure.<br>Provide information and direct support to SMEs on the benefits of the planned green public procurement policies. | Establishment of the Ukrainian Startup Fund (USF) providing grants and support programmes to start-ups.<br>Participation in Horizon Europe to fund research and innovation.<br>Creation of Diia.Business portal, an online hub providing information and hosting trainings for Ukrainian entrepreneurs.<br>The EEPO's development of a network of Diia.Business Support Centres.<br>Provision by private and state-owned banks of finance for green investments. |

## Context

### *Economic snapshot*

Ukraine's economy is facing the toughest challenges of its recent history. COVID-19 caused a 3.8% decline in GDP in 2020 and, although the economy began to recover in 2021 (Box 14.1), Russia's war of aggression against Ukraine in February 2022 inflicted severe damage, with civilian casualties in the tens of thousands, millions of people displaced within the country or abroad, significant infrastructure damage, trade disruptions and deep economic shocks (Box 14.2). As a result, real GDP shrank by 29.1% in 2022 (Table 14.3). Nevertheless, the economy showed considerable resilience: the full-year outcome was better than the 40-50% contraction projected at the start of the invasion and the economy largely stabilised after the first few months of the war. In mid-2023, real GDP growth estimates for the year stood in the 2-3% range (IMF, 2023[1]).

In 2022, exports of goods and services dropped by around 43%, while imports volume declined by 28%, owing to blocked transport routes (IMF, 2023[1]). The "Black Sea Grain Initiative" revitalised foreign trade by unblocking key seaports in the Black Sea, thereby improving access to international markets for Ukrainian agrifood companies, but Russia withdrew from the agreement in mid-2023. The transport issues represented a major challenge to Ukraine's business sector, and in particular to SMEs, which have fewer resources and logistical opportunities. Since May 2022, the EU has mobilised EUR 1 billion for the "Solidarity Lanes" initiative to increase global food security and support for the Ukrainian economy (EU NeighboursEast, 2022[2]).

Over 40% of Ukraine's SMEs had to stop or limit operations during the first weeks of the war (EBRD, 2023[3]). However, most Ukrainian SMEs adapted to the difficult situation, and only 6% of them had suspended operation by the end of the year (EBRD, 2023[3]). Their swift adaptation owed much to a successful transition of their business online and to a lowering of production capacities (EBRD, 2023[3]). Ukraine's banking system has also demonstrated great resilience, supporting uninterrupted electronic payment operations. However, the enterprise sector continues to struggle, and in early 2023, the share of non-performing loans (NPLs) had grown by 8 percentage points on the previous year, to reach 38%, reversing the stable trend of gradual reduction observed since 2018 (National Bank of Ukraine, 2023[4]).

Ukraine's international partners have provided military, humanitarian and direct financial aid to support the functioning of the government. Foreign budget support had reached USD 32.1 billion by the end of December 2022 and remains vital in 2023, as Ukraine's budget deficit is expected to be more than USD 38 billion. The IMF and the Ukrainian authorities estimate financial assistance needs between USD 36 and USD 48 billion in 2023 to ensure macroeconomic stability, maintain key public services and restore critical infrastructure (European Commission, 2022[5]). The support package also envisages critical reforms in the areas of rule of law, good governance and anti-corruption (European Commission, 2022[5]).

The Ukrainian government has prioritised digitalisation through the creation of the Ministry of Digital Transformation in August 2019. In 2020 alone, the share of online retail trade had almost doubled, jumping from 1.2% to 2.1% of total retail turnover. The IT sector has held strong even during the war; in fact, in 2021-2022, information and communication economic activities generated 4.7% of Ukraine's GDP, compared to around 3.8% in 2016. In 2021, export of IT services reached USD 7.1 billion, more than one-third of the total volume of exported services and one tenth of total exports, with 285 000 specialists employed in the sector. In 2022, the export of IT services increased by 5.8% year-on-year, reaching USD 7.5 billion. Electronic public services have also been developed, becoming widely accessible for all citizens and businesses. Digital government is one of the key recovery priorities.

## Table 14.3. Ukraine: Main macroeconomic indicators (2018-2022)

| Indicator | Unit of measurement | 2018 | 2019 | 2020 | 2021 | 2022 |
|---|---|---|---|---|---|---|
| GDP growth* | Percentage, year-on-year | 3.5 | 3.2 | -3.8 | 3.4 | -29.1 |
| Inflation* | Annual percentage increase, consumer prices | 10.9 | 7.9 | 2.7 | 9.4 | 20.2 |
| Government balance[1]* | Percentage of GDP | -2.1 | -2.1 | -5.9 | -3.6 | -16.7 |
| Current account balance** | Percentage of GDP | -4.9 | -2.7 | 3.4 | -1.9 | 4.9 |
| Exports of goods and services** | Percentage of GDP | 45.3 | 41.0 | 39.0 | 40.6 | 35.8 |
| Imports of goods and services** | Percentage of GDP | 54.0 | 49.1 | 40.5 | 42.0 | 52.0 |
| FDI net inflows** | Percentage of GDP | 3.7 | 3.3 | 0.0 | 3.7 | 0.2 |
| General government gross debt*** | Percentage of GDP | 60.4 | 50.5 | 60.5 | 48.8 | 81.7 |
| Domestic credit to private sector*** | Percentage of GDP | 34.5 | 30 | 28.2 | 23.6 | 23.5 |
| Unemployment[2]*** | Percent of total active population | 8.8 | 8.2 | 9.5 | 9.8 | - |
| Nominal GDP* | USD billion | 130.9 | 153.9 | 156.6 | 199.8 | 160.5 |

[1] General government net lending/borrowing. This balance considers grants received from IMF and other internal donors as part of revenues.
[2] Modelled International Labour Organisation estimates.
Source *(IMF, 2023[1]); ** (National Bank of Ukraine, 2023[6]); *** (World Bank, 2023[7])

### Box 14.1. Support for SMEs during the COVID-19 pandemic

In response to the COVID-19 pandemic, the Ukrainian government put in place various measures to help businesses stay afloat, such as loans, grants, subsidies and tax relief.

***Financial support***

In May 2020, the government revised the Economic Stimulation Programme to provide anti-crisis measures to facilitate access to finance for SMEs. Financial assistance has been provided via the Business Development Fund (BDF). Other initiatives included:

- The "5-7-9" State Programme was extensively used to help SMEs and entrepreneurs. The main instruments were credit guarantees and partial compensation of interest on the loan. In 2020, the programme granted Ukrainian hryvnias (UAH) 16.5 billion in credit and loans to 6 957 SMEs.
- To promote the vaccination campaign and support the most affected businesses, in December 2021 the Ukrainian government launched a special state support programme called *eAid (ePidtrymka)*. Under this programme, individuals who completed the full vaccination cycle could open a virtual bank account through the Diia portal and receive 1 000 UAH (~25 EUR), which could be spent only to purchase selected goods and services (e.g. books, gyms, cinemas, concerts).

***Regulatory flexibility***

The government supported SMEs and women during the pandemic through:

- Credit holidays: a special grace period for servicing loans during the quarantine for the population and businesses.
- Tax reductions: businesses were exempted from paying certain taxes during the quarantine.

***Workforce support***

Partial unemployment assistance was provided for SME employers and employees of SMEs. Quarantine-related changes were introduced into the Labour Code to regulate the new reality of remote work, flexible schedules and salaries.

***Market support and measures to improve access to digital infrastructure***

The Diia.Business platform was introduced at the beginning of the pandemic to provide online services and training. The platform uses digital learning methods based on short videos and short learning modules. Diia.Business also prepared several publications on doing business during the pandemic (business cases, fundraising). Several online courses were developed in co-operation with international organisations and the private sector, including:

- "Ten steps to start your own business", as well as courses on starting a business in a few sectors, such as textiles, ceramics, food manufacturing and technology.
- *Grow up: Agro* to support businesses in the agrarian sector.
- Financial literacy courses, including subjects such as accounting, taxation, reporting systems, marketing and other skills.
- An anti-corruption courses within the framework of the United Nations Global Compact in Ukraine's Anti-Corruption Collective Action programme.

Source: (Diia, 2023[8]).

## Box 14.2. Economic consequences of Russia's full-scale invasion of Ukraine

### *Infrastructure*

The direct damage on physical infrastructure in Ukraine was estimated at nearly USD 150 billion (EUR ~142 billion) by April 2023, which comprised damage inflicted upon:

- the residential sector (USD 54.4 billion/EUR ~51.4 billion), with nearly 158 000 destroyed buildings
- infrastructure (USD 36.2 billion/EUR ~34.2 billion)
- enterprises' assets (USD 11.4 billion/EUR ~10.8 billion)
- the education sector, surpassing USD 9.1 billion (EUR ~8.6 billion), with the number of damaged or destroyed educational facilities at 3 200
- energy infrastructure (USD 8.3 billion/EUR ~7.8 billion)
- the healthcare sector (USD 2.7 billion/EUR ~2.6 billion), with 806 healthcare facilities damaged or destroyed, including 367 hospitals and 341 clinics.

### *Migration*

By May 2022, 8 million people had been internally displaced in Ukraine, another 8 million had been recorded across Europe, and more than 5 million Ukrainians had been registered for temporary protection or similar national schemes. By mid-2023, Ukraine's military successes had allowed substantial return flows, but the UN agencies estimated that there were still 5.1 million internally displaced and 5.9 million refugees abroad as of July. This represents a huge challenge for local consumer demand and the labour market.

### *International trade*

Ukraine's traditional export and import routes (air, shipping and land-based) have been significantly disrupted since the invasion. Black Sea cargos previously constituted approximately 80% of total export volume and 50% of total imports volume (January 2022). Following the blockade of major seaports, Ukraine relied on small ports on the Danube River and on road and rail transport, but those rapidly became a bottleneck for large cargos, severely disrupting of the export of grain and other foodstuffs. Nevertheless, in 2022 Ukraine managed to increase its services exports, in particular in the field of telecommunications, computer and information services (40.5% of total services exports), transport (32.3%) and business services (11.2%).

### *Business sector*

In December 2022, power cuts hit the largest energy-consuming industries, such as metalworking, the chemical industry and machine building. As a result, 89% of manufacturing enterprises had to suspend operations temporarily. Enterprises lost 23% of total working time. While industries that supply basic human needs (food and light sectors) have been resilient, microenterprises were hit hard, with a 31% loss of working time. Most companies installed backup power sources, but they are probably less available for micro and small enterprises (e.g. only 44% of microenterprises vs. 90% of large ones).

Sources: (EU Council, 2023[9]; Kyiv School of Economics, 2023[10]; National Bank of Ukraine, 2023[11]; UNHCR, 2023[12]; Ukrstat, 2023[13]).

### *SME sector*

Ukraine's SME definition has not changed since 2012. The definition broadly aligns with EU criteria in terms of employment and turnover but does not include a balance sheet criterion (Table 14.4). The State Statistics Service of Ukraine (Urkstat) uses both the legal definition and a definition based on employment, to allow for comparability with EU countries.

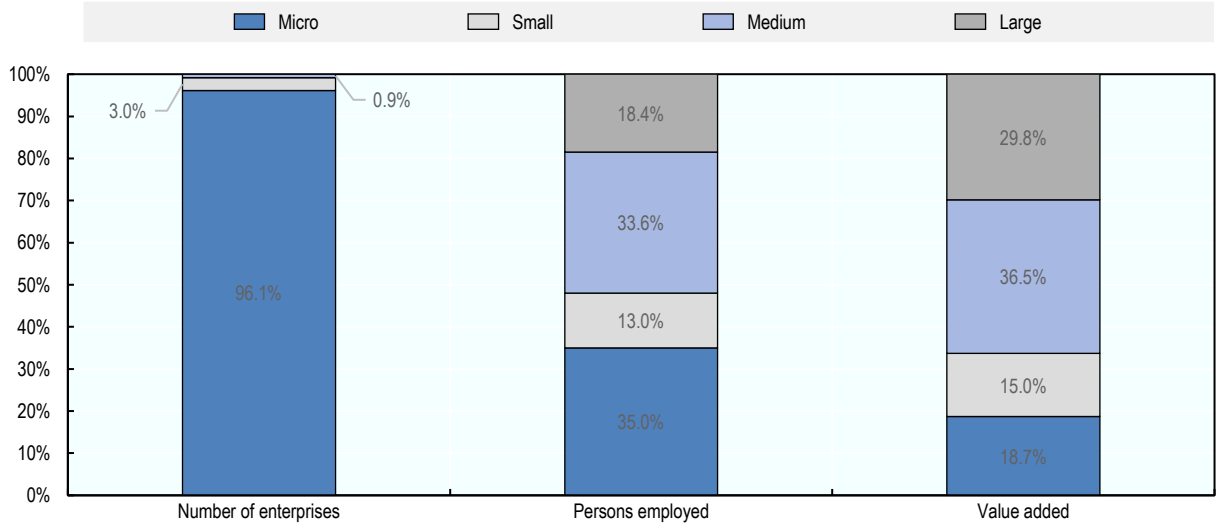
## Table 14.4. Ukraine's definition of SMEs

| | Micro | Small | Medium | Large |
|---|---|---|---|---|
| Employment | ≤ 10 employees | ≤ 50 employees | All enterprises that do not fall into the category of small or large enterprises | ≥ 250 employees |
| Annual income | ≤ EUR 2 million | ≤ EUR 10 million | | ≥ EUR 50 million |

Source: Commercial Code of Ukraine Art. 55, as of 22 March 2012.

In 2021, SMEs made up 99.9% of all enterprises in the business sector; 96.1% of them were microenterprises. SMEs accounted for 81.6% of total business employment in Ukraine and generated 70.2% of value added at factor cost in the business sector (Figure 14.2).

## Figure 14.2. Business demography indicators in Ukraine by company size (2021)



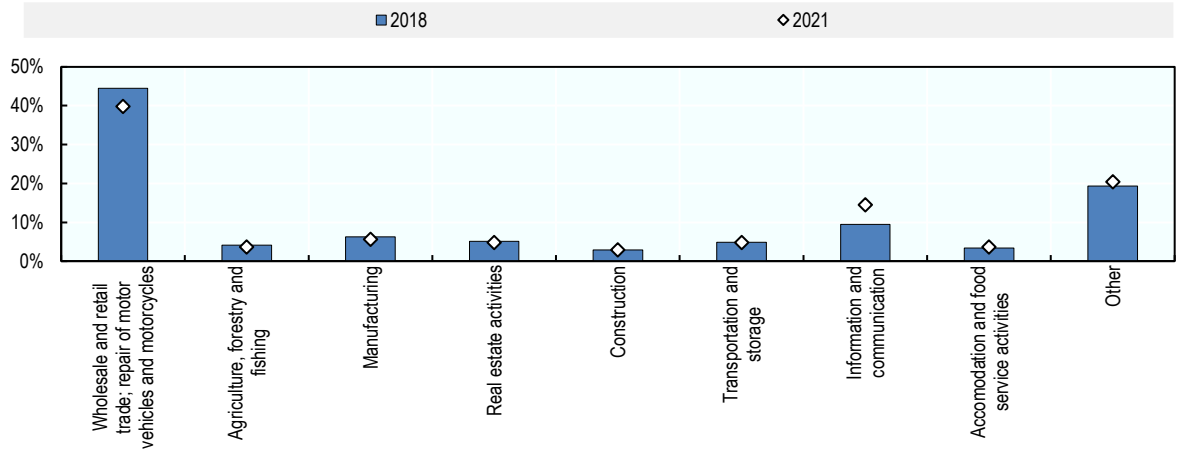

Note: The value-added at factor cost distribution was computed with 2020 data.
Source: (State Statistics Sevice of Ukraine, 2023[14]).

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The majority of SMEs in Ukraine still operate in wholesale and retail trade (39.8%) and thus remain concentrated in low-value-added sectors. However, recent years have seen a growing number of SMEs in the ICT sector, at 14.5% in 2021 versus 9.5% in 2018 (Figure 14.3).

### Figure 14.3. Sectoral distribution of SMEs in Ukraine (2021)

Share of SMEs by type of economic activity




Source: (State Statistics Sevice of Ukraine, 2023[14]).

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## SBA assessment by pillar

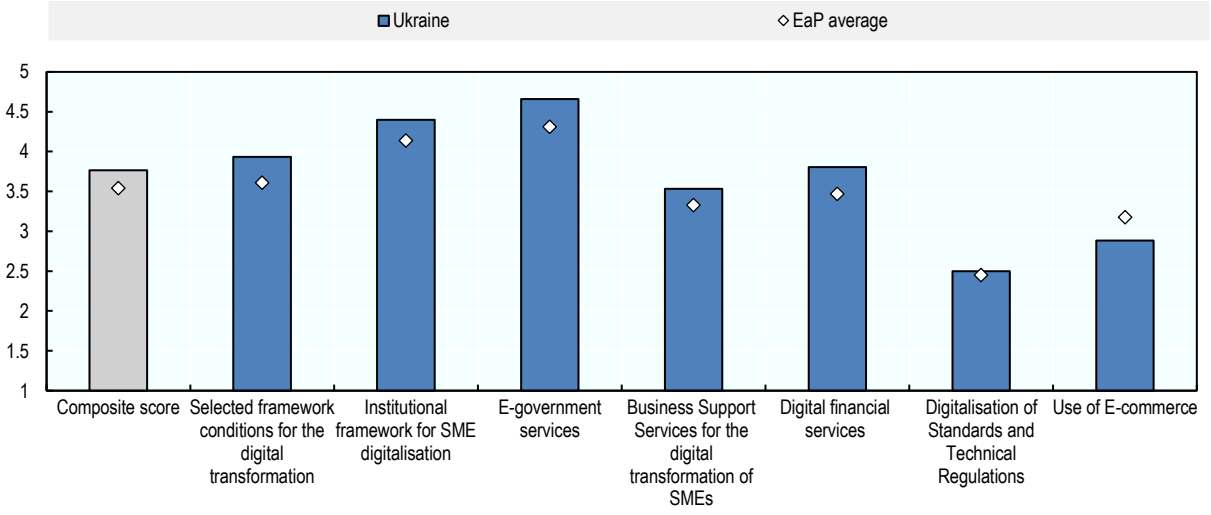
### *SME digitalisation policies*

Creating an environment conducive to the digital transformation of SMEs requires a comprehensive policy approach based on sound framework conditions for the digital economy as well as targeted support to help SMEs reap the benefits of digital solutions. Framework conditions refer to pre-requisites for the digital transformation, such as affordable access to high-speed broadband, a satisfactory level of digital literacy among citizens, and a well-coordinated and coherent policy approach and governance system for digital policies. In the context of SME development, those fundamentals need to be complemented with specific business support services, digital financial services for SMEs, and tailored support to engage in e-commerce to reach new markets.

Reflecting the multi-faceted nature of the topic, this round of SBA assessment evaluates EaP countries' policy approaches to SME digitalisation through i) a dedicated pillar on selected framework conditions for the digital transformation, as well as ii) six new sub-dimensions, incorporated in the pre-existing dimensions of the SBA assessment, to delve deeper into specific thematic policies to foster the digital transformation of SMEs. The weighted average of the scores for the new pillar and digitalisation-oriented sub-dimensions results in a composite score for SME digitalisation policies presented below (Figure 14.4).[1]

Ukraine performs slightly over the regional average, with a composite score of 3.77 for SME digitalisation policies. The assessment reveals strong achievements in building sound framework conditions for the digital transformation as well as institutional setting for SME digitalisation in particular. Ukraine also appears as regional top performer in terms of e-government services, thanks to the widely praised Diia initiative. More could be done to develop comprehensive support for the digital transformation of SMEs in non-IT sectors, and notably to help them reach new markets through e-commerce. Digitalisation of standards and technical regulations is addressed in an action plan, but implementation is still to follow.

## Figure 14.4. Scores for SME digitalisation policies in Ukraine




Note: Further details on the assessment and calculation methodology can be found in the "Assessment framework" section in the Digital Economy for SMEs chapter, in the "Policy framework, structure of the report and assessment process" chapter and in Annex A. Additional information on institutional framework for SME digitalisation and e-government services can be found in Pillar A; on digital financial services in Pillar C; on use of e-commerce in Pillar D; and on Business support services for the digital transformation of SMEs in Pillar E.

StatLink https://stat.link/rv8efo

The following section details Ukraine's performance in developing selected framework conditions for the digital transformation, while more information on digitalisation-oriented sub-dimensions can be found in the sections on the pillars they respectively belong to.

### *Selected framework conditions for the digital transformation*

Individuals and firms, notably SMEs, cannot fully reap the benefits offered by the digital transformation without the existence of robust framework conditions, such as comprehensive digitalisation policies, access to high-speed Internet and well-rounded ICT skills among the population. Accessible, affordable and stable broadband connection is indeed the *sine qua non* to ensure widespread participation of citizens and businesses in the digital economy, and to stem the widening of the connectivity gaps between urban and rural territories, and between firms of different sizes. Furthermore, fostering digital skills development at all stages of life through formal education and lifelong learning initiatives for adults is essential to help the working-age population acquire the skills they need to embark on the digital transformation, produce tech-savvy consumers, and build a talent pool of IT specialists.

#### *National digital strategy*

Ukraine does not have a single document as a National Digital Strategy. It has, however, been working on developing a strategic vision for its digital transformation: a Digital Agenda for Ukraine 2020 was developed to align Ukraine's digitalisation with EU standards. It was followed by the adoption of a *Concept for Development of the Digital Economy and Society 2018–2020*. Digitalisation currently features prominently in different key policy documents (Table 14.5): the National Economic Strategy 2030 (NES 2030), for instance, defines *digital economy* as a key priority for Ukraine's economic policy (Direction 18. Digital economy). Additional aspects of the digital transformation are mentioned in the *Strategy for Implementation of Digital Development, Digital Transformations and Digitalisation of the State Finance Management System for the period until 2025* (Strategic Goals 1-32). Provisions concerning digitalisation are mentioned

in the *Strategy for Digital Transformation of the Social Sphere* and in *State Regional Development Strategy for 2021-2027*. This document focuses on infrastructure development and digital transformation of the regions. There is also a *Strategy on the Integration of Ukraine into the European Union Digital Single Market* (the "Roadmap"). Notwithstanding Russia's ongoing war, Ukraine is pursuing and stepping up its digitalisation efforts, and developing plans for post-war recovery, with digital transformation constituting a thematic pillar of the draft Recovery Plan (National Council for the Recovery of Ukraine, 2022[15]). Ukraine's current approach also emphasises artificial intelligence (AI), with substantial efforts to align with the EU AI Act and to develop an adequate regulatory framework to this end.

### Table 14.5. Policy framework for the digital transformation in Ukraine

| Policy document and timeframe | Status | Main objectives | Selected measures |
|---|---|---|---|
| Concept for Development of the Digital Economy and Society 2018-2020 | Different action plans approved | Endorse priority areas, initiatives and digitalisation projects developed under the Europe 2020 Strategy. | Adoption of the Action Plan for the Implementation of eServices Development Concept for the years 2019-2020.<br><br>Adoption of the Action Plan on the Implementation of the International Open Data Charter Principle.<br><br>Approval of the Action Plan on the Implementation of a Cybersecurity Strategy in Ukraine in 2018. |
| Strategy on Integration of Ukraine into the European Union Digital Single Market ("Roadmap") 2018-2023 | Ongoing | Break down barriers and create new uniform rule on online services freeware distribution, most notably in digital marketing, e-commerce and telecommunications, and to strengthen the cybersecurity of networks and information systems. | December 2020: The Law on Electronic Communications which implements the EU Electronic Communications Code synchronously with the EU member states.<br><br>December 2021: Law on NCEK (National Telecom Regulator).<br><br>September 2022: The Law on Official Statistics.<br><br>December 2022: The Law on Amendments to Certain Legislative Acts of Ukraine on Ensuring the Conclusion of an Agreement between Ukraine and the European Union on Mutual Recognition of Qualified Electronic Trust Services and Implementation of European Union Legislation in the field of electronic identification.<br><br>June 2023: The Law on Protection of Consumer Rights. |
| Strategy for Digital Transformation of the Social Sphere<br>Since 2020 | Ongoing | Ensure European standards for the functioning of social protection institutions, the provision of social services, the financial stability of the social sphere, increasing its transparency and optimising its administrative expenditures.<br><br>Create a unified information environment of the social sphere.<br><br>Help the government contribute to social cohesion through the use of digital technologies. | Creation of a unified information base of the social sphere.<br><br>Unified register of providers and recipients of social services and benefits, as well as the introduction of a system verifying them.<br><br>"eBaby" (implemented 2020-22) to simplify the procedure for receiving services related to childbirth.<br><br>Web portal of electronic services of the Pension Fund of Ukraine providing remote services through the personal accounts of citizens and employers. |
| Strategy for Implementation of Digital Development, Digital Transformations and Digitalisation of the State | Ongoing | Solve the problem of the lack of integration between the information from the online public financial management system, the lack of a | Centralising the IT resources and IT functions of the Ministry of Finance and central executive bodies; priority is given to the centralisation of cloud technologies, the creation of a single data |

| Policy document and timeframe | Status | Main objectives | Selected measures |
|---|---|---|---|
| Finance Management System 2021-2025 | | single data warehouse with up-to-date information available to all public authorities, the obsolescence of individual platforms and the lack of automated information exchange with many other government agencies | warehouse and the gradual transition to a new level of service-oriented systems by ensuring the availability of public services online.<br><br>Creating a Committee of Information Technology Management in the Public Finance Management System.<br><br>Developing co-ordination and co-operation processes with the Treasury, the State Tax Service, the State Custom Service, the State Audit Service, and the State Financial Monitoring Service.<br><br>Regulating the functioning of the Unified Information and Telecommunications System of the public financial management system. |
| State Regional Development Strategy for 2021-2027 | Ongoing | Ensure economic growth, facilitating regional development, and preventing corruption.<br><br>Enhance unity and foster a decent life for citizens in a united, decentralised, competitive and democratic Ukraine. | Providing financial assistance to underdeveloped regions through financial support.<br><br>Directing subsidies and state aid mainly for creating of capital construction objects (state investment exclusively in state or communal property).<br><br>Strengthening the integrating role of agglomerations and large cities and thereby creating a legislative framework for the functioning and development of agglomerations, ensuring a balanced development of the territories that are part of them. |
| National Economic Strategy 2030 | Ongoing | Offer a coherent vision regarding the strategic course of Ukraine's economic policy by defining the long-term economic vision.<br><br>Develop Ukraine's digital economy as a main driver of economic growth. | Increasing IT education in public educational institutions.<br><br>Raising the overall digital skills levels of citizens through private and communal initiatives regarding digital skills and non-formal education.<br><br>Improving telecommunication infrastructure through targeted support to commercially disadvantaged regions and efforts to bridge the digital gap between urban and rural areas.<br><br>Harmonising digital legislation by developing a draft law to make the necessary changes to the Law of Ukraine "About electronic commerce", ensuring the implementation of the Strategy of Integration to the European Digital Market of the EU, and supporting the development of local crowdfunding and the principle of "peer-to-peer" within the framework of the EU4Digital Programme. |
| Draft Recovery Plan | Under preparation | Overcome crises, including those caused by Russia's full-scale invasion.<br><br>Reconstruction and further development of the country.<br><br>The key development goals are to accelerate the economic growth of regions and territorial communities based on the effective use of | Developing public e-services.<br><br>Institutional development of digitalisation, e.g. through strategic planning for the development of the digital sphere of Ukraine until 2025.<br><br>Developing the Diia Centres network, e.g. by updating and filling the Diia Centres platform and improving monitoring and evaluation of the quality of administrative services. |

| Policy document and timeframe | Status | Main objectives | Selected measures |
|---|---|---|---|
| | | domestic potential, job creation, improved employment and the accessibility of public services. | Developing public electronic registers, optimising them and centralising support; introducing electronic interaction.<br><br>Improving the government regulation of the use of electronic trust services, creating favourable conditions for the provision and receipt of electronic identification services. |

Source: (European Commission, 2019[16]; Yanovska, 2019[17]; Cabinet of Ministers of Ukraine, 2021[18]; Tarasiuk, 2022[19]; Shulga, 2019[20]; The National Council of Recovery of Ukraine from the Consequences of the War, 2022[21]).

Ukraine has worked towards a multi-stakeholder approach for the design and implementation of digitalisation policies. It created a Ministry of Digital Transformation in 2019, responsible for digitalisation policies, and the minister was granted the status of vice prime minister in 2022. Further co-ordination efforts were provided through the development of special digitalisation units in most government bodies, with the establishment of a new position of chief digital transformation officer and deputy minister in each ministry. The aim was to ensure co-operation across ministries at national and regional levels.

The NES 2030 was developed with the involvement of experts, scientists, officials and people's deputies through the establishment of a dedicated working group headed by the prime minister. More than 500 participants from the public and private sectors contributed to its creation: representatives of more than 20 analytical centres, more than 30 business associations, 40 bodies of executive power, expert circles and civil society, and people's deputies. The Secretariat of the Cabinet of Ministers leads the design, implementation, monitoring and evaluation of the strategy. It ensures co-ordination among state institutions responsible for provisions on digitalisation, i.e. the Ministry of Economy, the Ministry of Digital Transformation, the Ministry of Development of Communities and Territories, and the Ministry of Social Policy (mainly within the Strategy for Digital Transformation of the Social Sphere).

The NES 2030 provides for monitoring the implementation of the strategy, according to the set targets. Initial plans foresaw the monitoring to be carried out on a single e-governance web portal, which would summarise information on the implementation progress and analyse the degree to which specific target indicators had been achieved in the reporting period. The Strategy for Digital Transformation of the Social Sphere also has target indicators for the implementation of the strategy. However, despite these provisions, Russia's war against Ukraine, the occupation of part of the territory and the need to restore the infrastructure in the de-occupied territories, are posing considerable challenges to monitoring and evaluating the results of the strategies.

Current strategies give limited consideration for the digitalisation of businesses. The NES 2030 mentions the need to develop digital skills among businesses and a shared technology centre to foster access to digital tools but it does not provide for a comprehensive approach for support to SMEs' digitalisation. Moreover, policy documents do not have any targets to evaluate progress on SMEs' digitalisation. The previous SME Strategy did not address this issue either.

Moreover, the implementation has been challenged by Russia's war: beyond the challenges encountered in monitoring and evaluation, the lack of and/or reallocation of funding and resources to implement the strategy might hinder its execution. For example, the budget allocated to the Ministry of Digital Transformation was lowered from UAH 1 351 million (EUR ~35 million) in 2022 to UAH 616 million (EUR ~16 million) in 2023; most of the funds were awarded to e-governance, but there has not been any funding for "priority digital projects". However, the Ministry of Digital Transformation works in close co-operation with international partners such as the United States Agency for International Development (USAID), the Swiss Agency for Development and Cooperation (SDC), the United Nations Development Programme

(UNDP), and various companies (e.g. Google, VISA, Microsoft), which provide financial resources for a considerable number of activities and initiatives.

Moving forward, Ukraine could build on its impressive progress to date by developing a comprehensive approach to SME digitalisation and including relevant provisions in policy documents, associated with measurable targets and funds – e.g. on support programmes tailored for businesses, e-commerce and digital security. Regarding policy implementation, the authorities could create co-ordination mechanisms that involve non-governmental stakeholders, who play a major role in shaping and supporting the implementation of digitalisation policies. This could take the form of a public-private working group meeting, for instance, as a follow-up to the one formed for the development of the NES. Additional co-ordination tools would also further lower the risk of overlap and duplication between the different policy documents covering digitalisation issues.

### *Broadband connectivity*

The government fully acknowledges the importance of broadband connectivity for the country's development. This is reflected in the NES, which includes targets to increase mobile and fixed Internet coverage and seeks to stimulate the deployment of 5G networks in large cities. It is also reflected in the State Regional Development Strategy for 2021-2027, which aims to have all Ukrainian schools connected to the Internet by 2027 (up from the 2019 baseline of 37%). Ukraine does not have a national broadband plan: the *Concept of Digital Economy and Society Development in Ukraine 2018-2020* envisioned the development of a dedicated *National Strategy for the Development of Broadband Internet Access.* The Ministry of Digital Transformation held public discussions in 2020 on a draft, but it was never officially adopted. However, in 2021, the Ministry of Digital Transformation approved the *Plan of Measures for the Development of Broadband Access to the Internet for 2021-2022*, which paid considerable attention to improve the legal regulation of access to broadband Internet providers, access to energy and transport infrastructure, the connection of social infrastructure institutions to fixed broadband Internet access, and the creation of a state platform that shows the state of development of Internet access in different regions of Ukraine (Cabinet of Ministers of Ukraine, 2021[22]). The results of the implementation are not publicly available, and a follow-up document has not yet been approved. However, the National Council for Recovery of Ukraine has included provisions for fostering access to high-speed Internet in the Draft Ukraine Recovery Plan, emphasising the topic's importance for the country's post-war recovery (National Council for the Recovery of Ukraine, 2022[15]). Moreover, multi-stakeholder meetings are planned to discuss improvements in access to broadband (Ministry of Digital transformation of Ukraine, 2021[23]).

The publicly available indicators on subscriptions, coverage and quality of service reveal that Ukraine has already achieved considerable improvements in broadband connectivity over recent years. It appears to be the EaP country with the sharpest increase in uptake, especially for mobile broadband subscriptions (+969% in 2015-20 vs. 81% on average across the region), and for fixed broadband (up 60% vs. 38% for the regional average).

Moreover, the authorities have worked in recent years to tackle digital divides between urban and rural areas – e.g. in the Strategy of Regional Development and the Plan for 2021-2022. The government notably provided subventions to local budgets for the implementation of measures to increase the availability of broadband Internet access in rural areas. Despite these efforts and sizeable progress, digital gaps persist across regions and firms – an urban/rural gap of 14.6 percentage points in 2021, somewhat above the EaP average and OECD/EU values. Ukraine also lags OECD and EU levels in terms of businesses connectivity, the size of the gap being negatively correlated with the size of the company.

Policy implementation has, of course, been hampered by the war; many of the initiatives of the government and the Ministry of Digital Transformation in the field of broadband connectivity have had to be postponed. Moreover, access to the Internet and the quality of data transmission have decreased due to Russian and Belarusian cyber and physical attacks. More than 4 000 base stations and 1.7 million fixed Internet lines

were fully damaged or destroyed, which represents about a quarter of all Internet networks in Ukraine and created significant losses for over 700 telecom companies. Since the fall of 2022, Ukraine has been experiencing planned and emergency power outages, which also hinders the stable provision of Internet access. However, Ukrainian providers have begun to modernise and switch to the use of fibre-optic cable. This technology allows access to the Internet even in the absence of electricity in the network if the provider uses generators at key nodes and subscribers connect the router to an uninterrupted power source (power bank or battery). The war has shown the resilience of Ukrainian Internet service providers, their flexibility and willingness to adapt to the war to provide Internet access in very difficult conditions. Satellites such as SpaceX's Starlink have also become part of the critical infrastructure, enabling quick restoration of communication in de-occupied territories and hospitals, schools, energy and social sectors. Progress was also made in terms of national and international roaming.

Moving forward, Ukraine should pursue its applaudable efforts in ensuring broadband connectivity for citizens and firms across the Ukrainian territory. The upcoming policy documents and measures should address the remaining digital divide in rural areas, and foster access to high-speed Internet in Ukrainian firms, especially small ones, as a very first step of their digitalisation journey. There will also be a need to restore Internet supply infrastructure in territories liberated from Russian occupation. When rebuilding (i.e. roads and other infrastructure), Ukraine should consider laying fibre at the same time.

### *Digital skills*

Despite the absence of a dedicated National Digital Strategy in Ukraine, digital skills development is addressed in several policy documents, framing Ukraine's efforts in that regard. The *Concept of Development of Digital Competences* (hereafter "the Concept"), adopted in 2021, sets overall guidelines for policy makers to develop the Ukrainian population's digital skills, defining key principles, approaches and objectives and suggesting actions (Cabinet of Ministers of Ukraine, 2021[24]). The NES 2030 also addresses this issue, with a strategic goal of *increasing the level of digital skills of citizens* within the Direction on Digital Economy, indicating that citizens' underdeveloped digital skills are holding back a full-fledged transition to the digital economy (Cabinet of Ministers of Ukraine, 2021[25]). The document envisages the implementation of online and offline digital education courses, support for private initiatives regarding digital skills in non-formal education, and the introduction of digital consultants who would raise citizens' knowledge on how to use fully digitalised services. In terms of the institutional framework, there are efforts at co-ordination on digital skills policies: for example, consultations were held with representatives of education institutions and the National Academy of Sciences of Ukraine to prepare the Concept. A National Skills and Jobs Coalition was reportedly created, as well as an Inter-Industry Council on Digital Development, Digital Transformations and Digitalisation.

Some 53% of the Ukrainian population was assessed as having digital skills that were below basic in 2019. Since then, considerable progress has been made in Ukraine in implementing a number of initiatives to foster digital skills development at all stages of life. With regards to the education system, digital competence is included as a key competence in the Basic component of preschool education and in state standards of both primary and secondary education. COVID-19 and the war in Ukraine have been forcing teachers and students to use online learning to ensure the safety of learning and access to education for people who were forced to evacuate and are unable to attend classes at school or university. Courses have been developed to improve teachers' digital skills. Moreover, several universities co-operate with IT firms, e.g. organising joint training event, seminars, and master classes.

A wide range of tools have been put in place to accelerate digital skills development among the population, in line with EU practices – making Ukraine the EaP leader in the field. Citizens can assess their level of digital skills with the online self-assessment tool Digigram, which has been developed for different target groups and already benefitted almost 700 000 users over the past two years (incl. over 200 000 teachers). The government of Ukraine used DigComp 2.1: The Digital Competence Framework for Citizens to create

the Digital Competence Framework for Citizens of Ukraine, as foreseen in the Concept (which also included the development of methodological recommendations for the application of this Framework). DigComp derivatives are also being developed for different target groups, such as educators and civil servants. Based on the Digital Competence Framework, the Ministry of Digital Transformation has launched a national online platform for the development of digital literacy, Diia.Digital Education, where Ukrainians can take free digital literacy courses and test their knowledge. The courses are designed in the form of an educational series, where the topics of the courses are explained in short videos. Attendees can pass a test at the end and get their skills certified. Training is informal and corresponds to the concept of lifelong learning.

The regular collection of granular data enables monitoring, an element also emphasised in the Concept. Ukraine is one of the most advanced EaP countries in terms of digital skills assessment practices, as underlined in the EU4Digital comparative survey (EU4Digital, 2020[26]). The Ministry of Digital Transformation conducts nationwide surveys to monitor the dynamics of the population's level of digital skills. Such data have been collected twice so far (in 2019 and 2021), and show improvements: according to the survey, the share of Internet users increased from 88% to 92%, while the number of Ukrainians whose digital skills are below the basic level decreased from 53% in 2019 to 47.8% in 2021. The survey also illustrated the significant impact of COVID-19 on the use of Internet services: 52% of respondents indicated that they tried digital tools for the first time during the pandemic (online shopping, paying utility bills online, etc.). Overall, the significant improvements in Ukraine's digitalisation path have been reflected in international rankings such as the Network Readiness Index 2022, where Ukraine leads its income group – with strong performance on digital literacy.

However, more remains to be done, as Ukrainians' digital skills remain below OECD/EU levels. Building on the inclusion of digital competence in national curricula, students' progress in acquiring the different skills should be systematically assessed to ensure quality of education. Like EU practices, digital competence frameworks will also need to be regularly updated based on scientific research and stakeholder feedback to ensure their continued relevance, taking into account rapidly changing skills needs. Moreover, more could be done to promote digital skills among entrepreneurs and employees in non-IT sectors. Ukraine should finalise its Digigram version for entrepreneurs as well as the specific digital competence framework and ensure recognition of acquired competences to foster the employability of beneficiaries. The country could also develop reskilling and upskilling opportunities to tackle the remaining skills mismatches and help citizens meet labour market demand. Indeed, despite the booming IT sector, the lack of digital skills is still a major obstacle to SME digitalisation, as most companies cite the lack of experienced employees and expertise as a barrier to their digital transformation (35% and 31% of survey respondents, respectively) (German Economic Team, 2021[27]). Finally, additional data could be collected on the digital skills of SME managers and employees, and skills anticipation tools could be further developed: there are no regular digital skills forecasting exercises, and skills anticipation remains overall limited to some labour market forecasts, whose results are not publicly available.

## *Pillar A: Responsive Government*

### *Institutional and regulatory framework*

Ukraine has made progress in strengthening the institutional framework for SME policy since the last SBA assessment; however, this positive momentum has been disrupted by Russia's invasion of Ukraine. The government has reacted to the emergency by focusing on assistance to enterprises operating in strategic sectors and increasing the functions of the dedicated platform Diia.Business, which serves as a communication channel between the government and businesses and as a provider of essential administrative services to SMEs. Over the medium term, EU candidate status entails an agenda for institutional and regulatory reforms and an incentive to adopt good practices, while providing the basis for an enlarged programme of EU financial and technical assistance.

### Institutional setting

The implementation of Ukraine's first SME Development Strategy (2018-2020) has come to an end but no new strategy has been introduced. As a result, the country lacks policy documents that comprehensively cover SME-related issues. A new SME strategy should be adopted at the end of the war, in line with the priorities of the reconstruction plans and the EU accession roadmap and after assessing the extent of the damage to the country's productive capacity.

As for the actions taken before the war, it is important to note that in March 2021, Ukraine approved the NES (see above), which contains Direction 17 on entrepreneurship (Development of entrepreneurship). The strategy sets five strategic goals for entrepreneurship development: 1) ensuring an effective state policy on the development of entrepreneurship; 2) stimulating the development of an entrepreneurial culture and competences; 3) establishing conditions to increase the level of access to finance; 4) creating conditions for increasing enterprises' access to markets; and 5) stimulating innovations development. The NES also identifies a number of priority sectors such as ICT, agriculture and food production, hospitality and creative industries, all characterised by a high SME presence.

Although the NES does not have an action plan with time-bound targets or allocated funding, it envisages "target indicators 2030" for each direction. Most of the target indicators for entrepreneurship are declarative. Specific targets related to Direction 17 on entrepreneurship include improving Ukraine's ranking in the Global Competitiveness Index (from 73rd to 40th place) and the Global Innovation Index (from 45th place to 30th), financial and economic literacy training for 10 million citizens, and the growth of venture funding for Ukrainian start-ups (from USD 510 million to USD 5 billion). Nevertheless, there are no specific interim targets that correspond to specific actions.

The Ministry of Economy remains the central body in charge of developing and implementing SME policy, including SME support programmes and infrastructure, entrepreneurship promotion, and other SME-related issues. As digital transformation became a key national priority, the government established the Ministry of Digital Transformation in 2019.

The government also reorganised the state bodies that implement SME support policy. In autumn 2018, the Ministry of Economy established the SME Development Office (SMEDO), a donor-funded advisory body employing external private consultants. In addition, in the same year, within the framework of a donor-funded project, the government established the Export Promotion Office (EPO), a state institution to support Ukrainian exporters. In 2021, the agency was transformed into the Entrepreneurship and Export Promotion Office (EEPO), which *de facto* is now in charge of SME policy implementation as well as export promotion. The EEPO is accountable before the supervisory board, which includes both the Ministry of Digital Transformation and the Ministry of Economy. The agency, together with the Ministry of Digital Transformation, implements the national project for the development of entrepreneurship and export Diia.Business. The EEPO is in charge of the Diia.Business portal, which provides online trainings, consultations and other business support services (see below). Diia.Business has established a network of Diia.Business Support Centres where entrepreneurs can receive offline consultations.

The EEPO is fully operational and well-staffed. According to the Law on the State Budget, it receives funding as an export promotion institution. The 2023 state budget provides UAH 36.8 million (EUR ~1 million) for EEPO's activities. At the same time, its activities remain heavily dependent on international aid. In 2021, the institution received EUR 754 000 from donors, complemented by UAH 14.5 million (EUR ~475 000) from the 2021 state budget.

Despite the obstacles created by the war, EEPO has reached a high level of functionality and the Diia.Business platform is seen as an innovative instrument. In 2023, EEPO, together with the partners of the Consortium of the European Network of Enterprises in Ukraine, won the UkraineReady4EU Project in the European grant competition Business Bridge and attracted vouchers in the amount of EUR 3.75 million for 1 500 Ukrainian enterprises affected by the full-scale war.

In addition to supporting Ukrainian enterprises operating in the domestic market, EEPO focuses on the promotion of the export of goods, works and services of Ukrainian manufacturers, playing the role of a Trade Promotion Office (see below).

### Legislative simplification and RIA

The government is proceeding with the implementation of the deregulation reform that began with donors' support in 2015. In 2019, it approved a new deregulation plan, the "Plan of measures to deregulate economic activity and improve the business climate, an action plan to improve the conditions for doing business in Ukraine", that was set to expire at the end of 2022. In January 2023, the government extended the implementation time frame. The reform is ongoing, but the most important changes were introduced before the previous assessment (e.g. the last amendments to the RIA guidance introduced in 2016). The government also included deregulation in the NES 2030 under Direction 3 (Regulatory environment). However, the "target indicators 2030" only envisage an improvement in Ukraine's positions in international rankings. The deregulation plan targets both primary and subordinate legislation on regulatory requirements in different sectors. The ministries of Economy, Infrastructure, Regional Development, and Ecology and Natural Resources oversee the highest number of deregulation actions. According to the State Regulatory Service of Ukraine, 57 actions had been completed as of 21 January 2022 (e.g. the Ministry of Economy completed 19 out of the 32 planned actions).

In January 2023, the government established the Interagency Working Group on Issues of Accelerated Review of Instruments of State Regulation of Economic Activity. At that time, there were more than 1 000 regulatory instruments in place (including 528 permits, 224 licenses and 157 approvals). The first meeting of the working group recommended abolishing 47% of licenses and permits. Other licenses and permits must be mainly digitalised or amended. At the second meeting, in February 2023, the working group recommended abolishing or amending 90% of regulations managed by the Ministry of Environmental Protection and Natural Resources and government bodies under it. Such rapid decisions demonstrate that the government plans to foster deregulation efforts.

The State Regulatory Service of Ukraine (SRS) is the central body that executes state regulatory policy. According to the law, the SRS regularly reviews draft regulations and their RIAs. For example, in 2021, it reviewed 4 101 draft legal acts: 603 laws and regulations developed by central executive bodies, 64 draft regulatory acts developed by local executive bodies and 3 434 draft regulatory acts developed by local self-government authorities. In 2022, it reviewed 962 draft legal acts: 453 laws and regulations developed by central executive bodies, 24 draft regulatory acts developed by local executive bodies, and 485 draft regulatory acts developed by local self-government authorities. The RIA guidelines include the obligation to conduct RIA SME tests.

In 2020, the government officially launched the Diia portal, whichoffers multiple e-services that simplify regulatory procedures for SMEs. This is the most important change since the previous assessment. Entrepreneurs can start a business online (both legal persons and individual entrepreneurs), pay taxes, obtain permits and benefit from many other online services that reduce regulatory burdens. The government widely promotes the use of the portal and today Diia is one of the most widely used applications in Ukraine. At the same time, the government and local authorities support an extensive network of regional one-stop shops known as Centres of Administrative Services. According to the Diia portal, there are approximately 3 800 Centres and remote workplaces. Information on their location, contacts and infrastructures can be found on the Diia.Business portal.

### Public-private consultations

The Law on Basic Principles of the State Regulatory Policy in the Economic Activities Sphere mandates public-private consultations for the development of business-related draft regulations. The legislation does not limit forms of consultations but sets strict requirements about the time frame (a minimum of one month

and a maximum of three months from the date of publication). Formal and informal meetings between public institutions and the private sector are frequently held on an ad hoc basis, and the Ukrainian Business Council has played an active role in the elaboration of the NES. Nevertheless, there are no aggregated data on all public-private consultations in Ukraine, although government bodies and local authorities report on such consultations.

#### Institutional framework for SME digitalisation

At the moment Ukraine has not elaborated a strategic document on SME digitalisation. Promoting SME digitalisation is one of the objectives listed the National Economic Strategy 2030, under the broad objective of developing digital skills in the business sector. Strategic directions related to SME digitalisation include: 1) the implementation of eight roadmaps for digital transformation of key industries, including agriculture, machine building, tourism, light industry, food and processing, energy, mining, and defense; 2) the creation of new opportunities for the realisation of human capital, development of innovative, creative and digital industries and businesses; and 3) actions to make the development of creative, innovative and digital industries a main state policy priority.

Competence over SME digitalisation comes under the Ministry for Digital Transformation, operating in co-ordination with the Ministry of Economy, while EEPO is in charge of implementing SME digital transformation programmes. However, no funds have been allocated to those programmes given the current budget limitations.

The war has produced an acceleration of the digitalisation of the society and the use of e-government digital platforms (Diia, Diia.Business and Vzaemo.Diia), forcing SMEs to adopt digital tools. EEPO is supporting the digital transformation by proving online courses to SMEs. The Ministry of Digital Transformation of Ukraine is also working on promoting the application of AI technologies among businesses and in establishing AI governance rules, aligning them with those of the EU.

#### The way forward

Moving forward, the government should continue to elaborate short-term action plans for SME support to respond to the emergencies generated by the Russian invasion. At the same time, it should consider establishing a working group including SME representatives, local community representatives, and experts to elaborate a plan for the post-conflict recovery and reconstruction, looking at the role that SMEs could play in this phase, setting the basis for the elaboration of the country's post-conflict SME development strategy. To further strengthen the institutional and regulatory framework for SMEs, the government should continue to implement its deregulation plan under the National Economic Strategy 2030, focusing on the actions that could speed-up the reconstruction phase and the re-development of industrial sites damaged during the conflict.

### *Operational environment for SMEs*

Between 2020 and 2022, Ukraine made incremental progress on implementing the Economic Deregulation Strategy and the Public Administration Reform Strategy, with 94 actions completed so far. The most significant progress achieved is represented by the online provision of a wide range of administrative services to SMEs, in line with the country's digital strategy.

#### E-government services

Ukraine has actively promoted the development of a digital government in recent years. The main document in this field is the Concept of E-governance Development in Ukraine, approved on 20 September 2017. In addition, as mentioned above, the NES 2030 also defines the "digital economy" as a key priority

and includes relevant elements pertaining to government digitalisation. The Ministry of Digital Transformation is responsible for the development and implementation of e-governance policy.

In 2020, the government introduced the Diia.Business platform as a subproject of the Diia e-services ecosystem. The Diia.Business portal offers numerous resources to raise awareness among entrepreneurs on the available e-services. The portal provides information to SMEs on the availability of digital government services and instructions for using them. Ukraine continues to expand the list of services available online for SMEs. Some noteworthy ones include filing taxes or social security returns, pensions, the cadastre, reporting enterprise statistics, and the unified state register of court decisions.

The government also promotes the use of other digital platforms developed in the framework of the Diia project. In 2021, the government introduced the Vzaemo.Diia sub-project, designed to become an e-democracy instrument. The website included services such as e-consultations, e-surveys, e-petitions, and other e-democracy instruments. At the same time, the Ministry of Digital Transformation is transforming the mobile app Diia into a state "super app", constantly expanding its range services, including participation in polls and the possibility of executing tax payments.

It should be noted that local communities have already also used other digital platforms for public-private consultations, including E-Dem. The platform was developed within the framework of the E-Governance for Accountability and Participation (EGAP) programme, implemented by the East Europe Foundation in co-operation the Ministry of Digital Transformation and funded by Switzerland.

The "Resolution of the Cabinet of Ministers of Ukraine Approving the Regulations on Data Sets to be Published in the Form of Open Data", introduced in 2015, contains a formal requirement whereby government data should be "open by default". These requirements, however, have been suspended during the martial law.

Overall, Ukraine has made significant progress in the development of e-government. According to the United Nations E-Government Development Index, in 2020 Ukraine ranked 69th among 193 countries with a score of 0.7 points (United Nation, 2022[28]). In 2022, it had moved up to the 46th position with a score of 0.8 points. Despite all the challenges associated with the war, the Ministry of Digital Transformation of Ukraine continues to actively develop the open data sphere in Ukraine. According to the results of the Open Data Maturity 2022 EU report, Ukraine ranks second in Europe in terms of open data maturity (Carsaniga et al., 2022[29]).

### Company registration

Ukraine has made remarkable progress in simplifying and speeding up the company registration process. In 2016, according to the ABCA survey, the average registration time was 11 days. In 2021, business registration took on average 6.3 days (based on the Municipal Competitiveness Index, prepared by the Institute for Economic Research and Policy Consulting and USAID Competitive Economy programme). Nevertheless, the duration of the procedures depending on the size of the city, ranging from 3.6 days in Rivne to 14.4 days in Dnipro. Since 2023, enterprises have been able to register online through the Diia digital platform. The automatic registration consists of two steps: application submission and registration. The approximate time needed to complete the procedure is 11 minutes and it is free of charge. Online registration is available across the entire territory for natural persons (unincorporated enterprises), and since October 2020 for the registration of a limited liability company based on a model charter can be conducted through the Diia portal. Since 2021, all applications in electronic form for the registration of individual entrepreneurs are accepted through the Diia portal and only require a single step. As a further step towards the simplification of company registration procedures, since April 2021, the State Registrar is no longer required to check the documents attached to the online application to confirm the registration prior to the registration in the state register. Those functions are now performed automatically.

#### Business licensing

Business licensing is regulated by the 2015 Law on Licensing Economic Activities with Amendments. Information on licenses and permits' requirements is available on the Single Public Portal of Administrative Services as well as on the Diia portal, while a single interactive portal is under development. License applications can be completed online. According to Part 1 of Article 14 of the Law on Licensing, when a licensing fee is not established by law, it should amount to one living wage.

#### Tax compliance procedures for SMEs

SMEs view tax administration procedures as a burden on their activity. According to a survey conducted by the German Economic Team, in 2020, businesses spent on average 327.5 hours to submit and pay for the three main types of taxes (income tax, value added tax and employment tax, including contributions to social insurance). However, Ukraine has adopted a simplified tax system for SMEs since 1998 and efforts are under way to reduce the tax administrative burden. The current tax regime identifies four groups of taxpayers: 1) individual entrepreneurs whose annual income does not exceed UAH 1.1 million (EUR ~29 000) and who do not have employees; 2) individual entrepreneurs whose annual income does not exceed UAH 5.6 million (EUR ~145 000) and who employ less than 10 persons; 3) individual entrepreneurs or legal persons whose annual income does not exceed UAH 7.8 million (EUR ~203 000); and 4) individual entrepreneurs (farms) and legal persons whose agricultural production does not exceed 75% of total production. According to the simplified taxation system, each of the four groups is subject to a specific tax regime. Entrepreneurs falling under Group 1 pay a single tax up to 10% of the subsistence minimum. Those in Group 2 pay a single tax up to 20% of the minimum wage. Entrepreneurs and enterprises that are part of Group 3 are subject to a single tax set at 3% of total revenues for VAT payers and at 5% for VAT non-payers. Those under Group 4 pay a single tax calculated based on the type of agricultural land exploited.

The simplified tax system also envisages simplified accounting and filing rules. Tax declarations and tax payments can be filed and paid online. In 2022, the government introduced a number of changes regarding the single tax to support Ukrainian businesses of all sizes during the war. Almost all businesses (with a turnover less than UAH 10 billion or EUR ~260 million) became eligible to choose 2% single tax payments. Nevertheless, the government plans to abolish this instrument in 2023.

An enterprise must pay VAT when its sales amount to more than UAH 1 million (EUR ~26 000). The base VAT rate is 20%. According to a study conducted by the European Business Association, enterprises encounter problems with receiving VAT refunds, as 95% of the refund declarations are subject to checks.

#### The way forward

To further improve the operational environment for SMEs, Ukraine should 1) continue to implement the reform of company registration procedures, further reducing the time required to complete it and extending the application of the new procedures across the whole country; 2) calculate the effective tax rate applied to different types of individual entrepreneurs and SMEs, in order to identify potential distorting effects on enterprise growth of different tax regimes and incentives; and 3) introduce an automatic VAT refund system for all enterprises that present a low-risk profile for tax evasion.

### *Bankruptcy and second chance*

Insolvency proceedings in Ukraine are governed by the Code of Ukraine on Bankruptcy Proceedings effective since October 2019. While the new code introduced important elements (personal bankruptcy for individuals, more transparent sales procedures through e-platforms, etc.) enhancing its compliance with international standards (OECD et al., 2020[30]), it has also been the object of criticism. For instance, Engels, Biryukov and Chumak (2020[31]), in their EU-funded study, argue that Chapter VIII on foreign bankruptcy

proceedings is not in line the EU *acquis*. Moreover, contrary to the old law, the new code does not envisage provisions on out-of-court agreements, which are instead regulated by the Commercial and Procedural Code (Chapter V). Although many law firms have conducted different assessments of the insolvency framework (e.g. ENGARDE (2021[32]) and the EU-funded report by Engels, Biryukov and Chumak (2020[31])), no official review has been carried out recently.

Since the entry into force of the new Code, a significant number of events and campaigns directed to entrepreneurs fearing failure have been taking place. In 2020-21, the Ukrainian Bar Association, within the framework of the USAID "Financial Sector Transformation Project" and with the participation of the Ministry of Justice, implemented the project "Providing Advice on Restoring the Solvency of Individuals". The project entailed an extensive communication campaign involving leading Ukrainian media, as well as direct counselling (USAID, 2021[33]). In addition, several institutions, such as the Ukrainian Bar Association and the National Association of Insolvency Administrators, held annual forums to discuss issues related to bankruptcy.

Entrepreneurs seeking a fresh start can find useful information on the Diia.Business portal, including a checklist on how to restart a business (Diia.Business, 2023[34]). While these resources are mostly targeted to businesses that interrupted their activities as a consequence of the war, they also provide useful information for all entrepreneurs seeking a second chance. The Diia.Business portal also offers valuable resources for entrepreneurs to strengthen their entrepreneurship skills, including the ability to understand their needs and problems and identify and tackle financial distress. Relevant initiatives in this context are represented by the online course "10 steps to launch your own business" (Diia.Business, 2023[35]) which covers lessons on financial matters, and a web page presenting "the path of an entrepreneur" (Diia.Business, 2023[36]). In addition, it is important to mention that the government is currently working on a draft law to implement EU Directive 2019/1023 into Ukrainian regulation. This directive establishes minimum rules for EU Member States' preventive restructuring frameworks, with the aim of removing barriers to the effective preventive restructuring of viable debtors facing financial difficulties across the EU.[2]

However, there are no structured early warning systems in place and existing measures to prevent insolvencies are not being monitored and evaluated. Moving forward, Ukraine should consider further expanding activities to promote the rehabilitation of honest entrepreneurs, reduce the cultural stigma surrounding business failure, and develop measures to prevent insolvency.

## *Pillar B: Entrepreneurial Human Capital*

### *Entrepreneurial learning*

Ukraine has been making continuous policy efforts to promote entrepreneurial learning. The topic is addressed in the NES 2030 and in the Strategy of Development of High Education in Ukraine for 2022-2032, which includes entrepreneurial skills in higher education as one of its strategic goals.

Over recent years, Ukraine has successfully implemented a number of initiatives to foster the development of an entrepreneurial spirit and competences among citizens. The reform of the education system in 2016 and the approval of the Concept of State Policy "New Ukrainian School" by the Cabinet of Ministers marked a milestone. It notably embedded EntreComp and resulted in entrepreneurship being included as a key competence in the national education curricula at all levels of education – as highlighted in the 2020 SME Policy Index. The related Action Plan, approved in 2017 and running until 2029, defines targets for the development of entrepreneurial learning and paved the way for further progress. Additional documents have been adopted since the last assessment to foster the assessment of learning outcomes. For secondary schools, for instance, the State Standard of Basic Secondary Education, adopted in 2020, mentions entrepreneurship and financial literacy as a key competence that students should have acquired upon completion of the educational level. A Youth Entrepreneurial Competence Framework was also developed to help assess entrepreneurial competence. Moreover, Ukrainian schools continue to apply

innovative teaching and learning methods. For example, the project “Social school entrepreneurship”, implemented by Future Development Agency in Vinnytsia region since 2021, combines learning methods such as active learning and flipped classroom and is organised for lower secondary and upper secondary school students. In addition, the pandemic fostered the development of new online tools to enable distance learning. For example, in 2020 the All-Ukrainian Online School was created for students in grades 5-11 as a platform for distance and hybrid learning as well as a source of support for teachers, with video lessons, tests, and materials for independent work in 18 main subjects.

In higher education, entrepreneurial learning is further supported through several cases of co-operation between higher education institutions (HEIs) and businesses. Some companies organise courses for students and/or invite them to participate in business forums; for example, Deloitte provides special courses for students “Business through the eyes of the owner: From start-up to IPO”. In addition, ten universities benefit from a network of business incubators called “YEP”, a Ukrainian-Estonian entrepreneurship programme to develop start-ups among students. Diia.Business also launched the Diia.Business *Centre for Youth Entrepreneurship Development on the basis of Taras Shevchenko National University of Kyiv* to help students start their own business, notably through workshops, master classes, business conferences and educational events. However, these examples remain ad hoc – such events do not take place in all universities, and, while Ukraine has an increasing number of examples of co-operation between SMEs and general secondary schools, these practices are not yet widespread. Ukraine also supports lifelong learning and promotes entrepreneurship beyond education. A wide range of measures are being implemented to this end, by both public and private stakeholders.

However, progress regarding teacher training on entrepreneurial learning seems to have been rather limited since the last assessment, although some welcome steps have been taken. These include the ongoing development of additional learning materials, in co-operation with international donors such as Renaissance Foundation, and free online professional development courses, created in accordance with the requirements of the Procedure for Improving the Qualifications of Teaching and Research-pedagogical Workers. Teacher and manager training programmes were also approved in 2022 to implement the state standard of basic secondary education. However, the entrepreneurship key competence is still not compulsory in pre-service teacher training, and in-service teacher training programmes including entrepreneurship, approved by the Ministry of Education and Science in 2018, are only available in some levels of education (primary and lower, and upper secondary). The above-mentioned Action Plan does not foresee any actions to include entrepreneurship as a key competence in teacher training.

More generally, the existing policy documents in the field, e.g. the Action Plan, lack measurable targets. More could be done to ensure policy impact, building on previous efforts. Today, all learners do not engage in at least one practical entrepreneurial experience, despite some ad hoc initiatives, such as the annual business tournament “Company Strategy”. In terms of learning outcomes, even though entrepreneurial skills should be assessed, the State Standard of Primary and Lower Secondary Education in practice only lists the skills that school children should receive upon completion; it does not specify how exactly the teacher should assess them.

Moving forward, Ukraine could therefore complement its policy approach to entrepreneurial learning by strengthening pre- and in-service teacher training at all levels of education and promoting entrepreneurship in career guidance in high schools and university programmes. It could also improve monitoring and evaluation practices, ensuring learning outcomes are assessed and tackling the persisting lack of data, despite statistics being collected on VET and the employment of higher education students. Finally, co-operation could be further fostered between upper secondary schools and SMEs.

### *Women’s entrepreneurship*

Several strategies mention the development of women’s entrepreneurship, including the *NES 2030* and the *State Strategy for Ensuring Equal Rights and Opportunities for Women and Men for the Period up to*

*2030*, which notably aim at tackling women's overrepresentation in lower-level jobs, bridging the persisting gender pay gap and helping alleviate barriers to women's entrepreneurship. There is, however, no policy partnership to support women's entrepreneurship in Ukraine, which has traditionally been fostered by some initiatives within the framework of SME development projects. As of June 2023, Ukraine had not adopted any new SME support policy document, although the government plans on including a dedicated section on women's entrepreneurship in its next SME Strategy.

Despite the absence of a dedicated policy partnership, an extensive range of support services – including women-specific ones – have been developed for women entrepreneurs, often with support from international donors and private businesses, e.g. the recently launched an acceleration programme called "Vidvazhna" ("Brave"), which offers a three-month programme to women online and offline in ten Ukrainian cities. Moreover, Ukraine has made considerable progress in raising awareness about available support, as recommended in 2020: Diia.Business now serves as a one-stop shop, with a specific section on women's entrepreneurship. It lists ideas to inspire women to start their own business and various educational programmes – from generic courses for entrepreneurs (online school, "10 steps to launch your business") to women-specific ones such as the Visa-sponsored *She's Next* programme, which offers information on finance and accounting, implementing digital technologies, marketing, etc. It also mentions free online courses on digital entrepreneurship with support from the Netherlands.

Since February 2022, additional war-related support has been implemented, such as the *Women for the Future Programme*, which helps women who lost their jobs and/or income find new professional opportunities. USAID's Competitive Economy Program is also very active on the topic, and launched the West Business Hub, to help female entrepreneurs in war-torn regions relocate; a Business Resilience Platform offering online seminars with business advisory and psychological support; and mentorship sessions (Box 14.3). These various programmes are complemented by local private sector initiatives organised to promote women entrepreneurs and leaders – including, for example, the NGO International Embassy of Women Entrepreneurs in Ukraine – to unite women entrepreneurs across the country. It was established in 2016 in co-operation with a similar Polish NGO based on EU experience, and by the association Business Ukrainian Women.

### Box 14.3. Supporting women entrepreneurs through USAID Competitive Economy Programme (CEP)

USAID's Competitive Economy Program (CEP) in Ukraine is dedicated to fostering a robust, diverse, and inclusive economy, promoting growth among start-ups, SMEs, and competitive industries both domestically and globally. It strives to improve the business environment and facilitates international trade for Ukrainian companies, with IT, furniture, tourism, film and creative industries, and food processing receiving special focus from the programme. CEP achieves its objectives by providing grants to business support organisations, industry associations, and SMEs, empowering them with enhanced business knowledge, export skills, and access to finance.

USAID CEP in Ukraine carries out initiatives such as Women Biz Days and grant support, enhancing management, sales, and investment in women-owned businesses. From October 2018 to September 2022, 937 women-led enterprises benefited from the programme, generating USD 21.6 million in sales and USD 5.4 million in investment. Over 40 grants were allocated, creating approximately 1 600 new jobs. Women Biz Days' online seminars witnessed significant engagement, with 3 300 applications and 342 women owners graduating, reporting 95% improved self-efficacy. Post-participation, businesses saw a notable USD 1.4 sales increase with CEP support.

Since the outbreak of Russia's war, USAID CEP has stepped up its support through specific measures to help female entrepreneurs in war-affected regions, such as:

- The *West Business Hub,* which facilitates the relocation of female entrepreneurs from war-affected regions to safer areas, ensuring continuity in their business operations.
- The *Business Resilience Platform,* which offers online seminars to support women-owned and managed businesses in navigating the challenges of war, providing psychological and entrepreneurial adaptation and equipping them with knowledge for business scaling.
- The *Group Mentorship Sessions,* which offers legal guidance to up to 50 businesswomen and fosters a supportive environment for their professional growth.
- The *WIN Board Game*, which has developed a cognitive board game titled "Women in Leadership and Business" to promote leadership skills among female entrepreneurs.
- The *Updated Survey*, which builds on the "Portrait of Ukrainian Female Entrepreneur" survey with relocation and finance opportunities for women's entrepreneurship.
- The *Lviv-Kharkiv Creative Hub*, which encourages innovation and collaboration among creative brands led by female entrepreneurs.

Source: (Chemonics, 2023[37]).

Beyond specific support measures for women's entrepreneurship, steps have been taken to address the gender gap. The Ministry of Finance implemented a project on gender-responsive budgeting between 2013 and 2021, for example. The overall purpose of the project was to increase the economic efficiency and effectiveness of budget expenditures, considering the needs of men and women and their various groups. During the implementation of the project, changes were made to 25 normative legal acts to consider gender aspects in administrative and statistical reporting, as well as documents that regulate reporting in one or another field. Despite promising results, the project was suspended following Russia's invasion.

Despite these applaudable achievements, women entrepreneurs in Ukraine continue to face significant barriers to business development. Several studies offer valuable insights on women-specific challenges.

A survey from the Ukrainian Women's Congress, for instance, highlighted the considerable impact of COVID-19 on women: 38% of women-led enterprises saw a decrease in profitability, and 52% had to cease their activity. About 92% of female entrepreneurs believe that COVID-19 has had a negative impact on their business, with 40% of enterprises being forced to suspend their activities. Women entrepreneurs are also disproportionally affected by Russia's large-scale aggression, given the high share of women-led businesses in Donetsk and Luhansk oblasts. Almost two-thirds of internally displaced people are women and 83% of refugees are women (UNDP, 2022[38]). Beyond COVID-19, the Investment & Trade Facilitation Centre, in partnership with USAID, conducts annual surveys entitled "Portrait of a Ukrainian businesswomen", which provides data on the profile of women entrepreneurs in the country and information on the issues they encounter. The EEPO plans to collect additional data in the near future.

Overall, women entrepreneurs are still over-represented in low value-added sectors, tend to operate on a smaller scale, and do not engage in international trade, with only 7% exporting goods and/or services (Diia.Business, 2023[39]). They also struggle to access financing, with 63% of them having financed their business by themselves (WoMo, 2020[40]). Regarding gender equality in general, Ukraine ranked only 74th out of 156 countries in the World Economic Forum's Global Gender Gap Index 2021.

Moving forward, Ukraine could strengthen its strategic approach to women's empowerment and entrepreneurship by adopting a formal, national policy partnership, for example in its new SME Strategy. This could help co-ordinate efforts across the many public and private stakeholders involved. An impact evaluation of the different policies and programmes should also be carried out.

### *SME skills*

Despite the lack of a new SME Strategy and other policy documents comprehensively covering SME-related issues, Ukraine has made considerable progress in developing support for SME skills development since the last SBA assessment. The NES 2030 does touch upon entrepreneurship in a dedicated Direction (17), setting five strategic goals – including one on stimulating the development of entrepreneurial culture and competences", which contains several objectives related to developing entrepreneurial skills (including establishing an online consulting platform, disseminating best practices, implementing mentorship programmes). The target indicators include the establishment of an online one-stop shop that can provide information, training and consulting services for SMEs. However, most targets and objectives appear to be declarative, as the NES does define specific actions in these directions.

The implementation of these objectives started before the strategy was adopted: in 2020, the government launched Diia.Business, a subproject of the Diia e-services ecosystem, which became an online one-stop shop for entrepreneurial knowledge and consulting and appears as a good practice example. This led to Ukraine to widen its training provision to cover additional topics, as recommended in the 2020 assessment. The Diia.Business platform offers a wide range of e-training courses that cover different fields of business-related knowledge, more than 70 types of online consultations, and other business support services (see Box 14.4). Managed by the EEPO, the platform has successfully implemented innovative and user-friendly learning methods, such as short videos and learning modules (not more than 10 minutes), which are also available on smartphones. The Diia.Business platform also hosts the National Online School for Entrepreneurs, which contained, as of June 2023, 14 free, publicly available online courses. The courses cover a broad range of topics, including anti-corruption policy for SMEs, sustainable development, and digital transition. Specialised sections offer additional educational materials, notably on internationalisation (see also below),[3] social entrepreneurship,[4] and women's entrepreneurship (as mentioned above), as well as a self-test on personal data protection. Launched at the beginning of the COVID-19 pandemic, the implementation of Diia.Business and its classes benefitted from citizens' increasing interest in online services and training, fostered by pandemic-related containment measures. The platform now contains an increasing amount of information and support services to help businesses weather the consequences of Russia's ongoing war.

SME training provision strongly benefits from the considerable involvement of external stakeholders. Indeed, many online courses on Diia.Business have been developed in co-operation with international organisations and representatives from the private sector. USAID's Competitive Economy Programme, for instance, has been very active in developing programmes for early entrepreneurs,[5] as well as for women – including war-related support and sector-specific workstreams. Business associations provide additional support, either to help develop courses (e.g. the Ukrainian Business and Trade Association contributed to USAID's *Grow Up: Agro* programme), or by providing direct services. The Ukrainian Chamber of Commerce and Industry (UCCI), for instance, has a proven track record of providing training and advisory services, notably on internationalisation, legal issues and public relations (PR). This close co-operation with international donors and the private sector helps tackle the issue of the EEPO's limited resources (UAH 36.8 million, EUR ~1 million, allocated in the 2023 state budget), provides expertise, and fosters peer learning and the exchange of best practices.

Ukraine reportedly collects statistics on the uptake of such services, which, despite being only partly publicly available, enable monitoring participation: in 2021, 12 500 entrepreneurs attended the online school (EEPO, 2022[41]). As for Diia.Business, recent surveys demonstrate that businesses widely use it – according to the Institute for Economic Research and Policy Consulting, about 38% of exporters and importers used the Diia.Business platform in 2022 (up from 24% in 2021), and only 2% of surveyed businesses did not know about the platform. However, 57% of surveyed businesses declared knowing about it but not using it. Moreover, the EEPO collects feedback from participants on services and courses through automated surveys enquiring about user satisfaction and potential interest in other topics. This feedback then feeds into the development of new training programmes, which can help meet SMEs' needs and improve the overall quality of the support provided. For example, the EEPO designed the Export Academy 2021, a six-module training programme for SMEs based on inputs from participants of the previous *Train the Trainers* programmes (Pilot 2019 and 2020/21 editions). The pilot is supported by Estonia and the United States.

Despite these achievements, Ukraine still lacks an overall national framework for regularly collecting and analysing data on SMEs' skills. Ukraine does collect some data on in-house ICT training events, for instance, but there is no systemic approach to skills assessment and anticipation. There is no regular labour market analysis, nor survey on barriers to participation in trainings, even though these could complement recent efforts to assess SMEs' needs and significantly contribute to tailoring support services for SMEs and labour market requirements as closely as possible and to enhancing training uptake. Furthermore, the monitoring and evaluation of government-financed training for SMEs could be improved. The feedback collected so far is limited to participants' satisfaction, it does not capture the extent to which the services provided fostered skills development. The EEPO reported its intention to improve data collection and develop a new system to identify SME issues and gather insights on impact.

With regard to smart specialisation, Ukraine has planned additional steps to advance on its smart specialisation approach since the last assessment. The topic is addressed in the NES 2030 and in the *State Regional Development Strategy 2021-2027*. The latter document foresees several measures at the national, regional and business levels, notably emphasising the need to implement regional development projects designed based on the smart specialisation approach, and to develop SME support instruments in smart specialisation projects. However, these have yet to materialise; for example, SME-related support ( e.g. training) is not yet widely available (the EEPO is not engaged on the topic). Ukraine has requested all regions to conduct a mid-term review and adjustment of their regional development strategies, including the smart specialisation chapters, until 2027.

Moving forward, Ukraine could further develop its support for SME skills development by i) developing a systemic approach to skills assessment and anticipation, improving data collection and labour market analyses, conducting surveys on barriers to participation in training, and using additional tools to identify, monitor and forecast SME skills needs; ii) complementing its approach to collecting feedback by capturing

the impact of training on skills development and SME performance; and iii) further developing smart specialisation, e.g. by implementing targeted training for SMEs in the different priority areas.

### *Pillar C: Access to Finance*

Lending to the corporate sector has decreased since the last assessment, but the decrease has been significantly less pronounced than what might have been expected given the COVID pandemic and the war in Ukraine. Overall, the financial system has proven to be exceptionally resilient under the strain of the war. Both regulator and banks were quick in adjusting their operations to a wartime footing, and although there was a temporary shift toward short-term loans after the outbreak of the war, banks have managed to continue lending to the business sector. For SMEs, government support has been crucial to maintaining access to bank finance.

#### *Legal and regulatory framework*

The Ukrainian legal framework for secured transactions is based on a range of laws, including the Law on Collateral, the Law on financial restructuring, and the Commercial and Procedural Code of Ukraine. Since the last assessment, the framework has not changed, but its application has been heavily affected by the COVID pandemic and the war.

Following Russia's invasion, the NBU acted quickly to ensure the continued operation of banks in the country. It allowed banks to use cloud storage abroad (in the EU, UK, US and Canada) in order to strengthen the resilience of the banking system against attacks. It also put certain restrictions in place (in particular in relation to foreign currency transactions) and relaxed a number of regulatory requirements, including those on capital adequacy, liquidity, credit risk, reserve requirements and reporting. This has consequently led to a delay in the implementation of Basel III requirements. At the moment, the plan is to unwind emergency prudential measures by the end of March 2024, if the situation allows. Although NPLs seem to have stabilised over recent months, the full extent of losses for banks is not yet clear, but NPLs have risen to 39.1% as of June 2023 (National Bank of Ukraine, 2023[42]). According to the IMF, the NBU should now direct its efforts toward a review of banking assets to ensure appropriate action is taken so that financial sector stability is not compromised by high rates of default within a low-visibility environment (IMF, 2023[43]).

A cadastre and registers for immovable and movable assets exist. Previously, the cadastre was fully public and available online, but since the start of the war access must be specifically requested. Records of security rights over movable assets are managed through the State Register of Encumbrances on Movable Property, administered by the Ministry of Justice. Historically, enforcement has always been an issue and continues to be cumbersome and inefficient. According to a recent bank survey by EBRD, only one bank out of 25 surveyed deemed the enforcement of collateral (both movable and immovable) to be efficient. This is the lowest approval among all EaP countries (EBRD, 2021[44]). This issue will need addressing in the medium term to ensure that collateralisation works from beginning to end.

In addition to the Credit Register of the NBU, private credit information bureaus exist in the country. According to Doing Business data from 2020, the Credit Register covered less than 3% of adults, while the private credit bureaus covered around 56.9% of the population, suggesting significant room for improvement. From 1 January, the NBU will also collect information from non-bank financial institutions in its Credit Register, which should help boost coverage.

At the moment, financial institutions do not face any non-financial disclosure requirements. More generally, disclosure requirements have been rolled back even for more basic metrics and, understandably, the focus of the NBU has been elsewhere since the war began. This means, however, that there is no foundation yet for future reporting on ESG performance, green taxonomy or climate-related stress testing. The latter would be particularly valuable in an economy characterised by large-scale farming operations.

Ukraine's legal framework for capital markets is mainly based on the Law on Securities and Stock Market. The country has several stock exchanges, and the capital market infrastructure is fragmented. Bond issuances are dominated by government bonds, but larger-scale corporate issuances also exist. Upon the beginning of the war, corporate bond issuances plummeted from a monthly average of UAH 815 million (EUR ~21 million) (totalling UAH 9.8 billion or EUR ~253 million in 2021) to virtually zero from March 2022 until the end of the year 2022 (a few issuances happened in July, September and November). In 2023, issuances rebound strongly, however, with issuances for a total of UAH 11.9 billion (EUR ~307 mln) registered between January and August (National Securities and Stock Market Commission, 2023[45]).

### *Sources of external finance for SMEs (bank financing, non-banking financing, and venture capital)*

Commercial banks in Ukraine acted quickly to secure their operations and adapt their lending approach to the outbreak of the war. Thanks to previously implemented banking sector reform, swift action by the NBU, and good buffers built up before the war, the banking sector was able to weather the challenges it faced.

Overall demand by corporates decreased in 2022 after a brief peak in summer, initially shifting toward shorter-term loans and working capital financing. This trend has reversed since, with an increasing share of lending trending toward longer terms again (National Securities and Stock Market Commission, 2023[46]). However, interest rates remain elevated across all size categories of firms, which poses a serious problem for the affordability of credit.

At the same time, state-owned banks (SOB) have expanded their lending, and the share of loans to SOEs in total corporate lending has also ticked up in the course of the war from 7% in January 2022 to 8.6% in June 2023. This, combined with significant state support, has resulted in a marked increase in the state's role within the banking system in the wartime economy.

Government support has been mainly channelled through the 5-7-9 programme. Already during COVID, the programme was used to provide large-scale support to businesses under more lenient conditions than usual (e.g. full compensation of interest rates during lockdowns). Once the war started, the programme was again expanded to provide guarantees and interest rate subsidies to SMEs as well as companies in certain strategic sectors, such as agriculture, and for strategic purposes, such as the purchase of individual power generation capacity (wind and solar generators). As a result, corporate lending was highly dependent on the availability of the 5-7-9 programme, whose share in the overall corporate lending portfolio reached 26% (National Bank of Ukraine, 2023[47]).

The availability of non-bank financing products has largely dried up during the war. Microfinance is mainly provided through credit unions, which have been regulated by the NBU since June 2020. Since the beginning of the war, availability of funding through credit unions has plummeted to around 60% of pre-war levels, with the decline stopping for the first time in Q2 2023 (National Bank of Ukraine, 2023[48]). A new law on credit unions, passed in July 2023, has been a major step to improve the legal framework for microfinance. The law allows credit unions to provide a wider range of services to a broader pool of clients and allows for more diversified funding options for credit unions, which supports their financial sustainability. Changes to the Law on Deposit Guarantee Fund are being considered to allow credit unions to join, which would help the sector grow further. In addition, regulation in 2021 changed to provide more transparency and consumer protection. Since the change, microfinance must be provided on a fixed-rate basis, and providers are obliged to communicate the annual percentage rate (APR)[6] to clients.

Leasing activities are carried out on the basis of the Law on Financial Leasing. The law sets out clear definitions of lessor and lessee, as well as the rights and duties of both parties. Leasing is generally offered by major banks, and agricultural equipment is a common asset subject to leasing. The use of leasing has dropped significantly during the war, however, given that it relies on assets which are at risk of destruction. The legal framework for factoring is set out in the Civil Code (Chapter 73), as for many other countries in

the region, as well as the Commercial Code and Law on Financial Services. However, the law does not provide a clear definition of different types of factoring and does not allow for simple and clear assignments of present and future accounts receivable. In addition, factoring by electronic means is not possible, which inhibits the development of more scalable and efficient factoring solutions based on digital technologies that could make this type of financing more accessible for SMEs.

There is no specific legal framework for venture capital (VC). Instead, it is governed by the more general Law on Collective Investment Institutions (adopted in 2013), which does not provide a definition of venture capital. For earlier stage investments, a number of business angel associations exist that provide funding. A number of funds are also active in the country, but the majority of funding is still concentrated around the pre-seed and seed stages. A ban on investments by institutional investors means that the potential investor base is narrow. In addition, no government programmes exist to catalyse investments, for example, by topping up private investment, investing in VC funds directly, or establishing a fund of funds. Although the National Economic Strategy until 2030 mentions venture capital as an area to support, no specific measures or actions seem to be planned. VC investments had been steadily growing since the last assessment, to reach more than USD 800 million in 2021, with an expanding IT sector being an attractive target. Understandably, though, investments plummeted after the beginning of the war, and the future of the sector is highly uncertain at this point given the risks involved.

### *Financial literacy*

The NBU conducts assessments of financial literacy every three years, with the latest assessment prepared in 2021 in the context of the USAID Financial Sector Transformation Project. The results from the survey suggest an improvement vis-à-vis 2018. However, the gap in financial literacy between the urban and rural population has increased. General awareness for different financial products seems to be high, but usage is relatively low, and around a fifth of respondents turned to relatives and friends for money, indicating room for improvement when it comes to financial inclusion (National Bank of Ukraine, 2021[49]).The assessment looks at the general population, and does not have a module specific to entrepreneurs. While some information can be extrapolated from general assessments, it can be helpful to also test business specific skills in order to gauge gaps among small business owners and managers that could be addressed through targeted policy measures.

Financial literacy is taught in secondary school, which is important in terms of achieving broad outreach into the population. In addition, the aforementioned Diia portal provides a range of knowledge and training on financial literacy, accounting, and other potentially relevant topics to improve entrepreneurs' skills when it comes to finance, accounting and business planning. Having an accessible platform that brings together different resources is a very positive development as it can act as a one-stop-shop for businesses owners and managers to find the right public support for their individual needs.

### *Digital financial services*

The NBU's Fintech Development Strategy until 2025 was approved in July 2020. The strategy aims to support the development of a fintech ecosystem in the country and touches on important pillars, including awareness raising and financial literacy efforts, as well as the development of an open banking framework and a regulatory sandbox. However, it was superseded by a new Strategy for the Development of the Financial Sector of Ukraine in 2023, which contains objectives related to financial literacy and the open banking framework.

The NBU does not appear to have a dedicated department for dealing with issues related to digital financial services. The development of the Fintech and Financial Sector strategies was subject to broad consultations, which is very positive, especially when it comes to digital financial service provision. However, it appears that no institutionalised co-ordination or consultation mechanism exists in order to gather views from different public and private stakeholders when it comes to new regulation for the sector.

Such co-ordination is particularly important in the context of digital financial services as issues can touch on a range of topics which are not necessarily solely within the purview of the financial regulator.

#### *The way forward*

The NBU should continue its efforts to maintain financial stability and ensure the continued functioning of the banking sector, using necessary tools to evaluate the health of the sector and prepare for potentially required mitigating actions. In light of the expansion of state presence in the sector, plans need to be devised in order to ensure that this increased presence does not have adverse effects on the development of the sector. This applies both to the management of state-owned banks, and to the utilisation of public support programmes.

When it comes to the use of SME support programmes, notably the 5-7-9 programme, careful consideration should be given to defining a post-war role for them. Plans should be drawn up specifying how to adjust programmes in order to support the reconstruction effort and reduce the dependence on the state within the sector. In addition, it will be crucial to put in place adequate monitoring and evaluation mechanisms to ensure that funds are allocated efficiently and effectively.

Expanding the scope of sources for the collection of credit information could help improve coverage of the credit register or private credit bureau and allow a larger number of potential borrowers with a limited loan track record build up credit history. This would help individuals and firms access funding that have so far been excluded from bank financing.

The framework conditions for the secured transactions regime should be improved, with a particular focus on insolvency (creditor rights in reorganisation) and enforcement in the case of default. Enforcement mechanisms, both in and out of court, need to become more efficient to reduce the costs associated with bank lending.

When it comes to non-bank financing sources, efforts should be made to support the development of factoring and VC operations. Updating the legal framework for factoring could help address certain legal uncertainties related to this instrument, and allow for factoring by electronic means. This in turn would open the possibility of developing cheaper and more efficient factoring-based funding products that could help SMEs access affordable financing. For VC operations, once the situation allows, consideration should be given to developing public support mechanisms that can catalyse the sector, such as co-financing mechanisms or instruments like a fund of funds.

The development of regulation for digital finance is still at an early stage. It would be useful to have a dedicated focal point within the NBU, as well as a more institutionalised co-ordination mechanism to gather views from public and private stakeholders with relevant insights for the sector. In addition, linking up to international peers could help knowledge creation and learning from other regulators' experiences.

### *Pillar D: Access to Markets*

#### *Public procurement*

Since the latest assessment, as a result of pressures from the COVID-19 pandemic and the war against Ukraine, public procurement procedures have been simplified and their implementation better aligned with the principles of the EU Directives, with positive implications for SME participation.

Public procurement remains regulated by the Public Procurement Law (PPL) of 25 December 2015. It was reissued in a partly revised wording in 2019, followed by additional amendments and subsequent regulatory changes to align it more fully with the EU Directives on public procurement and address the challenges of the COVID-19 pandemic.

Some regulatory features commonly used to favour SME participation are in place, but rarely used (division into lots) or incomplete (use of a self-declaration of conformity with qualification requirements). As a temporary measure under martial law, public procurement is being carried out in one of three basic modes: 1) direct agreement (in a wider range of cases than under the PPL); 2) open tender (with shortened time limits and without e-auctions); or 3) purchasing of standard specification items of any total value using price quotations from the e-catalogues managed by several centralised purchasing bodies for medical supplies and by several centralised purchasing bodies for other items.

Recent changes relevant to SMEs include more extensive provisions on sustainable procurement (but still no firm obligation to apply them); the abolition of the tender committee system and the introduction of compulsory examination of persons authorised to carry out public procurement; and revised rules for fees charged by the review body, the Anti-Monopoly Committee of Ukraine (AMCU), to deter frivolous complaints against contracting authorities' decisions. In addition, there are more possibilities for the competitive participation of SMEs during the period of martial law due to the temporary changed thresholds for the obligatory use of open bidding procedure or e-catalogues:

- A lowered threshold for simplified procurement (direct agreement) from UAH 200 000 to UAH 100 000 (EUR ~5 000 to EUR ~2 500) for procurement of goods and services other than current repairs, meaning that more contracts now have to be procured by competitive procedures;
- UAH 200 000 for current repairs as a newly introduced threshold to address needs of the Ukrainian contracting authorising because of Russia's constant attacks on civil infrastructure and buildings (a "current repair" is a type of repair that is carried out with the aim of restoring the operational characteristics of building structures, systems and equipment to extend their service life); and
- UAH 1 500 000 (EUR ~39 000) for procurement of works (this threshold has remained unchanged).

The Ukrainian authorities continue to receive advice and support from the EU for further development of public procurement. In this context, a new medium-term public procurement reform strategy has been drafted and published for discussion. It includes new features intended to facilitate SME participation but does not set out any explicit objectives of support to SMEs in the public procurement system. Until its eventual entry into force, the roadmap for alignment with the EU Directives, adopted in February 2016, still applies. Also, Ukraine's SME Development Strategy 2017-2020 has not yet been followed by any similar document with due reference to public procurement, along with other related fields, although the NES 2030 mentions an objective to simplify SME access to public procurement (Ukrainian Cabinet of Ministers, 2021[50]; Ukrainian Cabinet of Ministers, 2021[51]).

Most public procurement is carried out through the ProZorro e-procurement system which has been in place since 2016, although its operation was suspended from late February to June 2022. It is complemented by the DoZorro system for monitoring public procurement. A lot of public procurement information is readily accessible through these systems. Available information indicates that SMEs make up 95 % of participants by number and account for more than 80% of total public procurement value.

Several of the shortcomings of the public procurement system identified earlier have now been mitigated by the procedural amendments mentioned above, favouring the participation of well-qualified SMEs offering quality goods and services and providing good value for money. Anecdotal evidence also indicates a general shift in attitudes towards greater attention to the importance of careful management of scarce public funds, with similar effect.

The still large number of contracting authorities, many of them small, means that there is a shortage of skilled procurement officials able to apply policies and practices that would favour SMEs, especially since many such officials are currently in exile. This problem is partly alleviated by the use of e-procurement, allowing officials to continue serving their contracting authorities even from abroad.

In these respects, the issues and the potential for improvement identified in the 2020 assessment report have been partly addressed. Nevertheless, further improving SMEs' participation will require continued

efforts, including 1) setting public procurement policy in a medium- and long-term development perspective and harmonising it with other policy measures, including those for SME development; 2) consolidating the improvements in attitudes, procedures and practices brought about by the pressures of the ongoing war; 3) continuing to enhance the functionalities of the e-procurement system for greater alignment with the principles of the EU Directives; and 4) improving procurement officials' skills in planning, preparing, awarding, and managing public contracts.

### *Standards and technical regulations*

There have been numerous achievements in the development of Ukraine's quality infrastructure and regulations. Regarding overall co-ordination and general measures, the country has progressed in its negotiations with the EU on the ACAA.[7] Several pre-assessments have taken place, and Ukraine is working diligently on further preparations to sign this agreement as soon as possible (European Commission, 2022[52]). The EU also acknowledged Ukraine's continuous pursuit of state policy reforms promoting a favourable business environment and regulatory framework, especially for SMEs. The Better Regulation Delivery Office continued with deregulation reform and improving the regulatory environment for businesses (European Commission, 2022[52]). Another achievement was the approval of the action plan for the development of Ukraine's system of technical regulation until 2025 by Ukraine's Cabinet of Ministers (executive order no. 1145-r).[8] Showing significant progress in the country's standards landscape, around 10 000 national standards developed before 1992 were replaced in 2019 (European Integration Portal, 2020[53]).

To support exports, particularly those of SMEs, the transformation of two Ukrainian offices was initiated to create the Entrepreneurship and Export Promotion Agency as a single SME support institution, and "Made with Bravery", an official electronic marketplace of Ukrainian products, was launched.[9] Several market surveillance measures are in place, and a strategy for market surveillance is also under development. An important aspect in this context is the EU's observation that "(t)he framework law (…) implementing EU Regulation 1020/2017 is not yet in place (and) funding of market surveillance authorities is also an issue" (European Commission, 2023[54]).

Regarding harmonisation with the *acquis***,** Ukraine has adopted 54 new technical regulations, resulting in 1) adopted legislation aligning with the EU *acquis* whose EU review is pending; 2) partly aligned legislation with the EU *acquis*; 3) adopted legislation designed to fully align with the EU *acquis* with pending EU verification not yet in force; and 4) legislation, for which further alignment is needed. Examples for group 1 are electromagnetic compatibility, low voltage, radio equipment, toys, cosmetics, machinery and pressure equipment. Examples for group 2 are lifts, cableways, gas appliances, explosive atmospheres equipment and simple pressure vessels. Further alignment under 4) is, for example, necessary in the fields of eco-design, energy labelling, and medical devices, while adopted legislation under 3) refers to construction products, see European Commission, 2023[10] for further details. Another accomplishment was that Ukraine's standards body, SE "UkrNDNC", became a CEN and CENELEC affiliate, a status that was approved in 2022 and entered into force in January 2023. This progress is also closely linked with UkrNDNC's Order No. 285 "On the package adoption of the CEN-CENELEC European regulatory documents by Ukraine" of December 2022. According to the document, Ukraine will adopt 20 268 European CEN/CENELEC normative documents as national normative documents by December 31, 2023.[11]

Although EU reviews of Ukraine's updated technical regulation to align itself with the EU *acquis* for various products are still pending, the country's overall SMEPI score on harmonisation with the EU *acquis* is almost identical to that of Georgia, which scored highest in the region on this sub-dimension.

Progress has also been made concerning Ukraine's approximation to the EU Digital Single Market Law[12] (European Commission, 2022[52]). Ukraine's legislation on metrology is in line with the *acquis*. However, further alignment of the metrology centres with the *acquis* is needed (European Commission, 2022[52]).

Concerning SMEs' access to standardisation, SE "UkrNDNC", aims to familiarise SMEs with the national standards via its website and standards catalogue. In addition, Ukraine has launched some basic support and training on standards and technical regulations for SMEs, specifically focusing on their integration into the EU Digital Single Market. No regular training events have taken place. Creating an action plan for education about standardisation is another action item for the future.

Regarding the digitalisation of standards and technical regulations, Ukraine has an action plan to digitalise public services. However, the digitalisation of metrology and market surveillance will require targeted measures in the future.

### *Internationalisation of SMEs*

Despite the extremely difficult circumstances, Ukraine continues to provide significant support to SMEs' internationalisation.

Until 2021, measures in support of SME internationalisation were implemented according to the Export Strategy of Ukraine 2017-2021, which included the creation of a favourable environment for SME export as one of its objectives. Although a draft proposal for a new strategy has already been developed (based on information gathered through a business survey) it has not yet been approved. In 2022, the government started working on an update of the Export Strategy. The development of the new strategy was informed by a survey conducted among Ukrainian exporters and industry and business associations. However, Russia's full-scale invasion of the country evidently brought a major shift in priorities and the approval of the draft strategy was put on hold. Nevertheless, discussions on this subject are expected to resume soon with the support of the International Trade Council.[13]

The main government bodies responsible for SME export promotion are the Ministry of Economy and the EEPO (formerly the EPO). In addition, the Ministry of Digital Transformation and the EEPO have launched the Diia.Business portal for the development of entrepreneurship, where entrepreneurs can access a wide range of support instruments. The portal includes a specific section devoted to export support through which businesses can access marketing, financial and legal assistance to export their products and services.[3,14] Standard forms of support provided include advisory services, an export-readiness online test, training and educational programmes, as well as sponsored participation at trade fairs and exhibitions. The government's financial support measures to foster SME export before Russia's invasion of Ukraine had yielded limited results. However, in 2022, the government started providing alternative financial support mechanisms through the Export Credit Agency (ECA) – e.g. by reducing insurance tariffs during the period of military operations. Yet, the list of requirements for the borrower are restrictive and a relevant number of enterprises is excluded (e.g. newly created enterprises).

It is also worth mentioning that in 2023, the European Commission has launched two calls for proposals under the joint title "ReadyForEU", which aim at helping Ukrainian entrepreneurs and businesses to benefit from the EU Single Market. The first component will provide financial support to Ukrainian SMEs affected by the war in the form of vouchers to access services and participate in trade fairs in the EU. The second component will allow new Ukrainian entrepreneurs to gain business experience in other European countries through the "Erasmus for Young Entrepreneurs - Ukraine" project (European Commission, 2023[55]). It is important to also highlight that Ukraine is the only country of the Eastern Partnership to be part of the European Trade Promotion Organisations Working Group of Information Professionals (ETPO-WGIP) and the Trade Promotion Europe (TPE). The former is a platform with a mandate for promoting exchange among European trade-promotion organisations in the area of information processing and dissemination. The latter is the European association representing the Trade Promotion Organisations and Agrifood Promotion Organisations of Member States to the EU institutions and Stakeholders. Finally, the project "EU4Business: SME Competitiveness and Internationalisation", commissioned by the EU and the German Federal Ministry for Economic Cooperation and Development and implemented by GIZ, has the

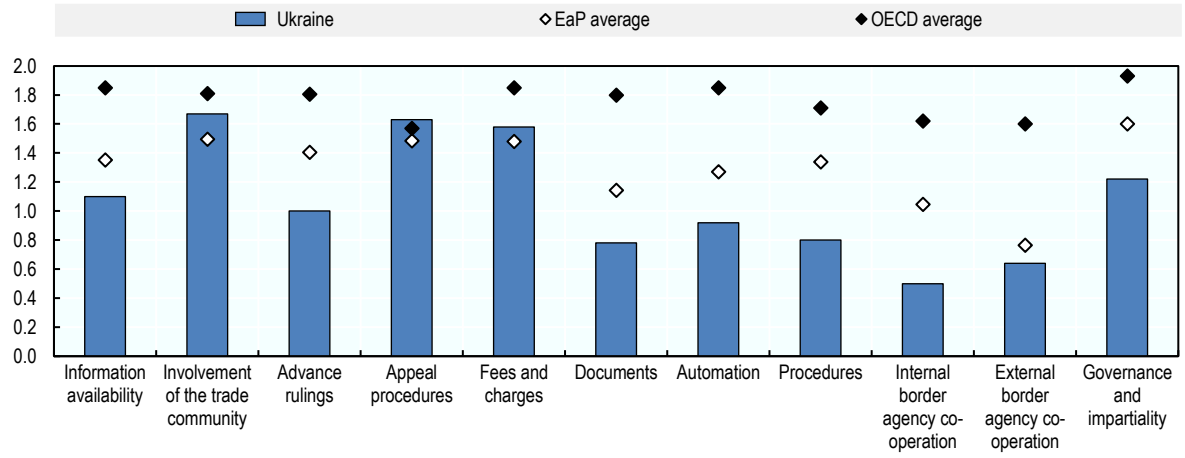
objective of creating better conditions for Ukrainian companies –in particular SMEs – to promote innovations and sell products on the European market.

Although support for the integration of SMEs into global value chains (GVCs) remains limited and there are no specific active programmes in this regard, in 2020 the Cabinet of Ministers of Ukraine adopted the Resolution “on the Approval of the State Programme to Stimulate the Economy to Overcome the Negative Consequences Caused by Restrictive Measures to Prevent the Emergence and Spread of the Acute Respiratory Disease COVID-19, Caused by the SARS-CoV-2 Coronavirus, for 2020-2022”, which includes finding opportunities for exporters to integrate into GVCs as one of its objectives. The programme also targets the development of innovative systems, including the transfer of technology transfer, and the simplification of hiring procedures for foreign highly qualified workers. Unfortunately, the programme is not operational and support to SME integration into GVCs is only at the initial stages. However, the Diia.Business project, as well as the several export promotion activities carried out by EEPO are helping SMEs become part of the global networks of production and trade. During 2020-23, about 2 500 Ukrainian businesses participated in 34 trade missions, 24 international exhibitions and more than 50 international B2B events. As a result, several businesses stipulated partnerships with foreign companies from all countries of the EU, United States, Canada, Great Britain, Turkey, Denmark, Sweden, Latvia, Lithuania, Estonia, Israel, UAE, and Qatar. In addition, the EEPO also carries out regular assessments of the changing global value chains in different sectors to help businesses identify priority export opportunities.[15]

E-commerce in Ukraine is regulated according to a number of laws and regulations, including the Law of Ukraine on Electronic Commerce, the Law on Payment Services, and the Law on Electronic Trust Services. This legal framework defines the organisational and legal principles of activity in the field of electronic commerce in Ukraine, establishes the procedure for conducting electronic transactions using information and communication systems, and defines the rights and obligations of participants in relations in the field of electronic commerce. Although the government of Ukraine has not developed a dedicated programme to promote e-commerce among SMEs, the Diia.Business portal offers multiple resources for businesses willing to sell their products online, mostly in the form of guidelines to access international e-commerce platforms such as Amazon, Etsy and Shopify.[16] Moreover, the Ministry of Digital Transformation of Ukraine, as well as the EEPO and Diia.Business are currently supporting “Made with Bravery” (shop.brave.ua), an e-commerce platform for goods made in Ukraine by Ukrainian producers. This new online marketplace, established in 2020, offers global delivery options and aims to facilitate international market access for Ukrainian businesses, particularly SMEs.

According to the last update of the OECD Trade Facilitation indicators, a large gap with both EaP and OECD countries remains. Improvements since the previous assessment have been marginal and a greater disparity with regional peers emerges in aspects such as automating and streamlining procedures, including harmonisation and simplification of documents, electronic exchange of data, simplifying border procedures, and internal border agency co-operation (Figure 14.5).

## Figure 14.5. OECD Trade Facilitation indicators for Ukraine, 2022




Note: Trade Facilitation indicators take values from 0 to 2, where 2 designates the best performance that can be achieved.
Source: OECD Trade facilitation indicators, https://oe.cd/tfi.

StatLink https://stat.link/ya5i2t

To conclude, despite an undoubtedly challenging context, the EEPO continues to provide outstanding support to SMEs and achieve its main targets. Moving forward, Ukraine could continue improving SME internationalisation support by ensuring the adoption of the new Export Strategy, increasing transparency (e.g. carrying out an independent review of the agency and publishing the list of beneficiaries of export promotion programmes), and expanding support programmes for the integration of SMEs into GVCs and the promotion of e-commerce.

### *Pillar E: Innovation and business support*

#### *Support services for SMEs and start-ups*

Since the completion of the SME Strategy 2020, Ukraine has not developed a new medium-term strategic policy document for the design and delivery of support services to SMEs. At the time of writing, work was underway to develop the next strategy. Understandably, Russia's invasion has forced the government to reprioritise its resources and policymaking efforts towards securing short-term emergency support for the business sector, rather than carrying out extensive analysis and policy consultations to plan for the medium term. Nevertheless, in March 2021, Ukraine approved the NES 2030, which contains a chapter on the development of entrepreneurship, with specific measures for enhancing the business support infrastructure and the provision of services to SMEs.

Notwithstanding the challenging war environment in which the government and its agencies have been operating since February 2022, however, implementation of SME support has continued and made important progress. The EEPO, under the joint supervision of the Secretariat of the Cabinet of Ministers, the Ministry of Economy, and the Ministry of Digital Transformation, is the main agency promoting the development and internationalisation of Ukrainian SMEs. The most important advancement since the previous SBA assessment is the creation of the Diia.Business portal as part of the broader *Diia* initiative, the government's ecosystem of e-services (see Box 14.4. Diia.Business).

Diia.Business has quickly developed into an information-rich and effective online one-stop shop for Ukrainian entrepreneurs. Rather than being simply an additional channel of communication of government-sponsored programmes, Diia.Business represents a genuine hub for SME support, through which the EEPO provides direct assistance to SMEs. It also integrates information on available support tools

managed by third parties, such as international donors, regional governments, business associations, and NGOs.

Diia.Business features a very advanced user experience, where the content is clearly structured around the needs of entrepreneurs. The main services available through the platform include online trainings on a wide range of topics, one-to-one consulting sessions, and information on financing opportunities (over 400 national, regional, and donor-funded support programmes published since 2021). Interestingly, the platform also contains a list of over 150 business ideas with basic information on how to start a business requiring minimal initial investment.

An analysis of the government's activities to stimulate a private market for business development services reveals a mixed picture. On the one hand, traditional governmental financial support for SMEs to cover (part of) the costs of professional advisory services remains unavailable,[17] although information on a similar scheme sponsored by EBRD is provided under the "grants" section of the Diia.Business website. On the other hand, however, the government seeks to leverage private sector actors to strengthen the infrastructure for entrepreneurship support in Ukraine in two ways. First, the EEPO is developing a network of physical Diia.Business Support Centres throughout the country (14 as of March 2023), which can be opened in partnership with consulting companies and business associations meeting certain logistical, technical, and financial requirements. Second, through the Diia.Business platform, the EEPO provides contacts, geolocalisation and a short description of services offered for a list of over 500 business support organisations (private and public) in the country.

Despite the important advancements to digitalise government services and improve the online ecosystem for business support, full-fledged government programmes to support SME digitalisation are not (yet) available in Ukraine. However, the Diia.Business platform hosts a series of trainings developed with private companies on various topics related to the digital transformation, such as how to transfer business processes online in wartime conditions (with the online education company IAMPM) and on social media marketing strategies and techniques (with Facebook). In addition, SMEs can get initial advice on digitalisation-related matters through the free online consultation opportunities described above, although this kind of support does not entail an in-depth analysis of the company operations and is unlikely to deliver a tailored roadmap for their digital transformation.

Moving forward, a strong SME strategic framework would provide more certainty and medium-term planning in implementing support programmes. Diia.Business Support Centres should also be monitored to ensure they deliver on their mandate to reach to rural SMEs, as regional disparities in business development services were highlighted in the EEPO's recent annual reports. Finally, compatible with available funding, the government could consider introducing grants to increase the focus on developing private business development services (BDS) providers (build on free consultations and introduce schemes to facilitate continuous access to it.

### Box 14.4. Diia.Business – Ukraine's one-stop-shop for SMEs and entrepreneurs

Ukraine's large-scale national project for entrepreneurship and export promotion Diia.Business was introduced in early 2020 by Ukraine's Ministry of Digital Transformation. As part of the Diia ecosystem of e-government services, Diia.Business provides services and information to support Ukrainian SMEs, both online and through offline activities. The project has been implemented by the EEPO since May 2021.

Diia.Business' online component consists of the Diia.Business website: a one-stop shop for entrepreneurs offering all essential information for each stage of business development, from ideas to promotion and accessing markets abroad. The web portal provides multiple e-services, including a list of over 150 business ideas, an online handbook as well as a national online school for entrepreneurs, templates of all necessary legal documents, free online consultations, a marketplace of financing opportunities and analytics of Ukrainian's business conditions.

The Diia.Business portal grants further access to information on the network of 13 offline support cenrers for entrepreneurs spread across Ukraine. In May 2022, Diia.Business's first centre abroad opened in Warsaw. In these locally operated and supported centres, Ukrainians can, inter alia, enjoy free consultations, educational commercial events, or test their products at special pop-up locations.

**How does Diia.Business contribute to SMEs' development?**

Ukraine's size is a challenge to providing local and comprehensive support to SMEs. Thus, in combining offline and online access to its services, Diia.Business gained national reach (and beyond since May 2022) and acts as Ukraine's main hub for entrepreneurship, concentrating all necessary information to maximise business development.

Furthermore, Diia.Business support centres are noncommercial public organisations that do not seek profit: 70% of the services are free while the income from the remaining 30% of services finances Diia.Business locations and employees. Launching and developing one's business has thus become significantly more affordable for Ukrainians.

Finally, the multiplicity of e-services available with Diia.Business has allowed for the simplification of regulatory procedures for SMEs and thus decreased the regulatory burden. Added to clear efforts to create user-friendly portal design (making the online platform easy to navigate and very intuitive), Diia.Business thereby makes entrepreneurship accessible to all, including on a practical and administrative level.

**What have been the results of the Diia.Business project?**

Diia.Business is today one of the most widely used applications in Ukraine. During the 2020-23 period over 6 million visits were made to the web portal (with more than 60 000 personal accounts set up) to browse sections on agrarian, women's, social and veterans' business. The popularity of Diia.Business most notably increased during the pandemic, and by the end of 2021 it had provided over 5,650 free consultations to entrepreneurs – used mostly for legal support, taxation, business planning and digitalisation.

In parallel, since the launch of Diia.Business, its support centres have had more than 89 000 visitors; its experts have held over 5 000 consultations in an offline format; and about ,500 educational events for entrepreneurs have been held in these centres and attended by 72 000 entrepreneurs. Several online courses have also been developed in co-operation with international organisations and the private sector.

Source: Diia.Business Website; EEPO Annual Report, 2024 SBA assessment questionnaire.

*Innovation policy for SMEs*

In late 2019, the government of Ukraine adopted the Innovation Development Strategy 2030 as its guiding document for innovation policy. Two years later it adopted its first Action Plan 2021-2023. While these documents do not contain explicit targets or a dedicated section for promoting SME innovation appear in these documents, the action plan contains several measures to support innovation activities in the SME sector, with a greater emphasis on export-oriented SMEs. As of early 2023, public information of the implementation status of the Innovation Development Strategy was not available, although the Ministry of Education and Science collects information from implementing bodies every six months and is planning an analysis of the strategy's effectiveness and implementation of the Action Plan later in later 2023. There is no dedicated innovation agency in Ukraine, and responsibilities for the design and co-ordination of innovation support policies are shared between the Ministry of Education and Science, the Ministry of Economy, and the Ministry of Digital Transformation, each with a leading role in the science, business, and digital sectors, respectively.

Governmental institutional support for innovation has seen some progress since the previous SBA assessment, although Russia's war has slowed down the implementation of the planned reform process. First, as a welcome step to build the evidence base for designing innovation support instruments, in 2020, the government conducted a survey among Ukrainian businesses (75% of which were SMEs) on current practices, needs and obstacles to perform innovative activities and invest in R&D.[18] Second, in 2021-22, the parliament adopted several laws to stimulate the development of industrial parks and manufacturing in the country, and even though 60 industrial parks were registered as of early January 2023, most of them are reportedly not active and the government did not allocate a budget to this area in 2022. Third, Ukraine has expanded its network of Technology and Innovation Support Centres (17 active in 2023), which help innovators with IP protection, IP agreements with partners and clients, and technology search. Fourth, in 2021, the Ministry of Education and Science launched a "Science2Business" platform, which encourages co-operation between the scientific and business communities by simplifying the search for partners, allowing businesses to request specific research and scientists to commercialise the results of their work.

Financial support for business innovation remains concentrated on the technology and start-up sectors, although there have been some developments in the last four years. The recently established Ukrainian Startup Fund (USF) promotes the creation and growth of early-stage technology start-ups through grants up to USD 10 000 (USD 35 000 in the case of dual-purpose technologies increasing Ukraine's defence capabilities) awarded via a competitive process. Specifically, to incentivise innovation in the defence sector, the government has also recently launched the BRAVE1 platform (brave1.gov.ua), collecting ideas and offering grants for the developments of military technologies. USF complements its financial support with access to accredited acceleration programmes where start-ups can benefit from training, mentoring and networking opportunities. In addition, the government has recently established Diia.City (city.diia.gov.ua), a dedicated legal and tax environment incentivising investment and employment for companies operating in the IT sector. Furthermore, although some indirect incentives (e.g. exemptions from corporate income tax and VAT payments) for investment covering R&D and business expansion exist in Ukraine, they appear to be designed exclusively for large companies (investment projects above EUR 20 million). Finally, Ukraine participates as an associated country in Horizon Europe, the EU's key funding programme for research and innovation (see Box 9.2).

On current practices for monitoring and evaluation, Ukraine's performance is rather mixed. Ukrstat, the national statistical office, regularly produces nationwide statistics on the innovative activities of enterprises following the methodology adopted by Eurostat in its Community Innovation Survey. This provides the government, and the broader community of innovation stakeholders, with a good set of outcome-oriented indicators to monitor the innovation performance of Ukraine's business sector, broken down by enterprise size. On the policy side, however, while some good examples can be mentioned (e.g. the Ministry of Education and Science's analytical reports in the area of technology transfer), important shortcomings

remain, in particular on the implementation of the Innovation Development Strategy, as well as on the impact of financial support mechanisms on SMEs' innovation performance.

Moving forward, the government could consider introducing new measures in favour of business innovation and industry-academia co-creation to move beyond the linear technology transfer model towards partnerships between academia and industry to jointly fund, manage and implement research activities (OECD, 2022[56]). Existing indirect incentives for innovation could also be adjusted so that SMEs can also benefit from them when investing in projects of a smaller scale than those of larger firms. Lastly, monitoring and evaluation could evolve to include impact evaluation of innovation-support initiatives, although an analysis of the impact of the innovation strategy on various sectors of the economy is promisingly included in the Ministry of Education and Science's planned activities for 2023.

### *SMEs in a green economy*

Russia's war has substantially challenged substantially Ukraine's progress in this dimension since the previous SBA assessment. The war damaged vast territories, contaminated land and water, and diverted policy makers' attention from the implementation of environmental policies, in particular for SMEs.

Ukraine currently lacks a strategic approach to supporting SME greening. The main documents with provisions on environmental policy in Ukraine are the "Law on Key Principles of the State Environmental Policy of Ukraine 2030" (and its National Action Plan 2025) and the NES 2030. While the former includes environmental issues as part of the broader economic policy and the NES 2030 considers green objectives at the sectoral level (e.g. energy, manufacturing, mining), neither of them contain specific provisions targeting SMEs, which may hinder policy effectiveness with smaller enterprises and with those that do not fall into the targeted sectors. The Ministry of Environmental Protection and Natural Resources is the main government body in charge of environmental policy.

Implementation challenges persist and are reflected in the updated scores for this dimension. They relate to the lack of dedicated funding allocations for the current National Action Plan, which raises uncertainty regarding the effectiveness of green/environmental policies in the medium term, and of an organisation with a strong mandate for SME greening. Furthermore, the government does not have dedicated financial support programmes or incentives to promote greening practices among SMEs. The scarcity of SME-focused environmental policies and support instruments translate into the low performance of corresponding monitoring and evaluation practices.

Ukraine has made some steps forward in promoting green practices through the advancements in green public procurement, the increased availability of green loans, the introduction of support instruments to improve ESG performance, and the activity of international donors. First, in 2020 the parliament introduced the notion of "life cycle cost" into the Law on Public Procurement, which allows contracting entities to consider the environmental impact of the procured goods or services among the tender assessment criteria. Second, both private and state-owned banks provide finance for green investments, particularly for the green energy transition (e.g. buying and installing solar or wind power stations and heat pumps), although the lack of SME-specific instruments raises questions on the extent to which such financing options are accessible to smaller entrepreneurs. Third, Diia.Business publishes a wealth of informational materials to increase SMEs' awareness about ESG risk factors, and a self-test that allows companies to assess their ESG readiness (including their environmental performance) and better understand where they should focus their attention moving forward. Lastly, donor-led initiatives, such as EU4Environment, EU4Energy, and EU4Climate continue to support the Ukrainian government in developing green economy policies and bridging the financing gap for SMEs, for instance by promoting better environmental governance, implementing resource-efficient and cleaner production practices, and providing vouchers for SMEs to develop green technologies and climate innovations. An example in this regard is the Climate Innovation Voucher initiative, implemented by the NGO Greencubator in 2022, through which 13 Ukrainian

companies received EUR 500 000 to adopt technologies that reduce greenhouse gas emissions, increase energy efficiency, and prevent climate change (Diia.Business, 2022[57]).

## Way forward

Ukraine continues to make impressive efforts to support SMEs despite unprecedented circumstances. To complement its current approach and further strengthen its SME policies, the government should consider the following measures:

- Ukraine could build on its impressive progress in the provision of digital government services to develop a comprehensive approach to SME digitalisation, supported by dedicated provisions in policy documents, measurable targets and funding, including support tailored for businesses, e-commerce, and digital security. The involvement of non-governmental stakeholders via co-ordination mechanisms can enhance policy implementation and prevent overlaps with other policy documents. Further efforts should address remaining digital divides, ensuring high-speed broadband connectivity for citizens and firms, particularly in rural areas. The restoration of Internet supply infrastructure in de-occupied territories should be accompanied by laying fibre. Finally, Ukraine could build on its achievements on digital literacy by systematically assessing student progress in acquiring digital competences, further enhancing digital skills among firms in non-IT sectors, finalising Digigram for entrepreneurs, developing re-skilling and up-skilling opportunities, and improving data collection and digital skills anticipation exercises.
- In Ukraine's drive to strengthen SME policy, the disruption from Russia's 2022 invasion led to a focus on aiding strategic sectors and enhancing the Diia.Business platform’s functionalities to facilitate vital communication. Leveraging the EU accession status presents an avenue for both institutional and regulatory reforms, reinforced by financial and technical support. Notably absent, however, is a post-war SME strategy aligned with reconstruction plans and the EU roadmap, resulting in incomplete policy coverage. Addressing this, the implementation of actions from the National Economic Strategy 2030, bolstered by intermediate targets, becomes a pivotal step for entrepreneurship promotion. Ensuring the continued roles of the Ministry of Economy and Ministry of Digital Transformation is crucial, alongside sustained operations of the SME Development Office and EEPO, supported by allocated resources. To enhance the business environment, Ukraine should prioritise deregulation via the Interagency Working Group and streamline State Regulatory Service reviews. Simplified procedures can be achieved via active promotion of the Diia web portal and Centres of Administrative Services. Lastly, transparency and accountability in public-private consultations, aligned with regulatory principles, remain paramount. In terms of fostering a favourable operational environment for SMEs, Ukraine should advance its digital government initiatives, expanding online services via the Diia.Business platforms, while standardising and streamlining business licensing and registration processes across cities. Tailored tax compliance procedures, along with online tax declaration options, should be adopted to accommodate diverse business sizes and activities. Addressing challenges related to VAT refunds is essential, necessitating a comprehensive review of refund processes for transparency and efficiency enhancement. Ukraine’s government should also sustain support measures for businesses during conflicts, including adaptable adjustments to single tax payments. Ukraine should further strengthen its insolvency framework and bankruptcy prevention measures by re-introducing out-of-courts agreements in the new Code, adopting structured early warning systems, and ensuring regular evaluation of insolvency-related measures. Finally, Ukraine should expand activities to promote rehabilitation of honest entrepreneurs following bankruptcy.
- Ukraine can enhance its approach to entrepreneurial learning by reinforcing teacher training for both pre- and in-service educators across all academic levels, and by promoting entrepreneurship in high school and university career counselling programmes. There is a need to refine monitoring

and evaluation methodologies, ensuring the comprehensive assessment of learning outcomes while addressing the persisting scarcity of data, despite the collection of statistics related to vocational and higher education students' employment. Collaborative initiatives between secondary schools and SMEs can also be further cultivated and broadened across the territory. To bolster its commitment to women's empowerment and entrepreneurship, Ukraine should consider the adoption of an official national policy partnership, which could be included in its new SME Strategy. This collaborative approach would harmonise actions among various public and private stakeholders. To evaluate the impact of policies and initiatives, comprehensive impact assessment should be undertaken. Ukraine's support for SME skills development could be further amplified by establishing a systematic approach to skills assessment and anticipation; improving data collection and labour market analyses; using additional tools to identify, monitor and forecast SME skills needs as well as evaluate training's impact on skills and SME performance; and fostering smart specialisation with targeted training for SMEs.

- To boost SMEs' access to finance in the longer term, Ukraine should clarify the role to be played by SME support programmes like the 5-7-9 programme in a post-war context. To allocate funds efficiently and appropriately, the government should draft detailed plans for adjustment and strengthen its monitoring and evaluation mechanisms. In parallel, the current lack of non-financial disclosure requirements calls for the development of a foundation for future ESG reporting, especially as Ukraine's economy is dominated by a large farming sector. Moreover, in the light of the recent disruptions in its economy, the Ukrainian state has increased its presence in the banking sector. Preventing the potential adverse effects of this intervention on finances necessitates that the government develops strategies in this direction and minimises exemptions to prudential measures. Additionally, the accessibility of the funding sources that are still not part of bank financing would be enhanced by broadening the scope of sources for the collection of credit information, which would thus improve the coverage of the credit register. Ukraine could also improve the functioning of enforcement mechanisms within the secured transactions framework. Non-bank financing in Ukraine should also be reinforced: the ongoing war has led to a significant decrease in both non-bank finance and investments, which has left the future of the sector in a highly uncertain state. It is therefore essential for Ukraine to update the legal framework for factoring and to develop support mechanisms that accelerate VC operations. Finally, while progress has been made towards enhanced financial literacy with the new Diia platform, Ukraine should also establish a department dedicated to digital finance services-related issues within the NBU to make advances in the elaboration of a regulatory framework for digital finance. Such an initiative should go hand-in-hand with more institutionalised co-ordination mechanisms and other measures to connect international stakeholders.
- Ukraine's public procurement faces SME-favouring challenges despite regulatory alignment with EU Directives. Despite the ongoing conflict, procedural simplifications under martial law led to more effective procurement, with modified thresholds enhancing competition and raising transparency. Further improvements are needed in long-term policy development, consolidating positive changes, enhancing e-procurement, and improving procurement officials' skills. Ukraine's progress in quality infrastructure and regulations includes negotiations for the ACAA and EEPO. However, challenges persist, such as incomplete framework laws for market surveillance and the need for more alignment with the EU *acquis*, especially in metrology. Adopting EU-based technical regulations, aligning metrology centres, and familiarising SMEs with standards, providing basic training, and digitising public services should be prioritised by the Ukrainian government. For SME internationalisation, Ukraine should prioritise the adoption of the new Export Strategy, loosen the requirements to access the financial support offered by the ECA, further improve the transparency of EEPO's operations, and expand SME support for GVC integration and use of e-commerce.
- Although EEPO's Diia.Business platform provides extensive support to Ukrainian entrepreneurs (thereby acting as a true hub at the centre of the ecosystem for financial and non-financial support

providers), it could further improve its offering by introducing a dedicated programme for SME digitalisation, considering dedicated grants to help SMEs access private advisors, and enhancing monitoring and evaluation mechanisms with an increased focus on impact evaluation. In terms of innovation policy, the government could consider introducing new measures in favour of business innovation and industry-academia co-creation, to move beyond the linear technology transfer model towards partnerships between academia and industry. Existing indirect incentives for innovation could also be adjusted, for SMEs to also benefit from them when investing in smaller-scale projects than larger firms. To advance on the green economy agenda, Ukraine should adopt a more strategic approach that features clear responsibilities and funding for assisting SMEs, considers dedicated incentives for helpinh SMEs adopti green technologies, and reinforces SME-oriented environmental policies.

## Table 14.6. Roadmap for policy reforms – Ukraine

| |
|---|
| **Strengthening framework conditions for the digital transformation** |
| • Develop a comprehensive policy approach for SME digitalisation with clear targets and funding, including dedicated support programmes, e-commerce, and digital security. |
| • Establish co-ordination mechanisms involving non-governmental stakeholders to enhance policy implementation and prevent overlaps with other documents. |
| • Prioritise broadband connectivity for citizens and firms in Ukraine, addressing the digital divide in rural areas and further supporting high-speed Internet access for small businesses. |
| • Restore Internet supply infrastructure in previously occupied territories and lay fibre while rebuilding roads and infrastructure. |
| • Ensure systematic assessment of students' digital skills and regular updates to digital competence frameworks. |
| • Promote digital skills in non-IT sectors, e.g. by finalising Digigram for entrepreneurs and by creating re-skilling and up-skilling opportunities to address skills mismatches and meet labour market demands, particularly in SMEs. |
| • Collect additional data on digital skills of SME managers and employees to inform evidence-based policymaking and labour market forecasts. Consider developing digital skills anticipation tools. |
| **Bolstering the institutional and regulatory framework and operational environment for SMEs** |
| • Develop short-term SME action plans for post-invasion emergencies; form a working group with SME, local, and expert input for recovery planning. |
| • Implement deregulation from the National Economic Strategy 2030 for swift post-conflict reconstruction, and industrial site revival. |
| • Systematically apply SME test in regulatory reform, considering RIA for enhanced SME impact assessment. |
| • Streamline company registration, reducing time and expanding nationwide. |
| • Assess effective tax rates for various businesses to uncover growth-affecting tax disparities. |
| • Implement automatic VAT refunds for low-risk tax evasion cases across enterprises. |
| • Reintroduce out-of-court settlements in the Code on Bankruptcy Proceedings. |
| • Establish insolvency prevention measures. |
| • Promote honest entrepreneur rehabilitation and tackle the stigma of business failure. |
| **Promoting entrepreneurial skills and women's entrepreneurship development** |
| • Complement efforts to improve entrepreneurial learning by strengthening teacher training across education levels, further promoting entrepreneurship in career guidance, and improving monitoring and evaluation practices. |
| • Strengthen women's empowerment and entrepreneurship via a formal policy partnership, co-ordination of stakeholders, and rigorous impact evaluation. |
| • Develop a systematic approach to skill assessment and anticipation, improving data collection and labour market analyses, as well as conducting surveys on barriers to participation in training and using additional tools to identify, monitor and forecast SME skills needs. |
| • Better capture the impact of training on skills development and SME performance by collecting feedback. |
| • Develop smart specialisation by implementing targeted training for SMEs in priority areas. |
| **Facilitating SME access to finance** |
| • Promote financial stability by minimising exemptions to prudential measures and developing plans to ensure that increased state presence in the banking sector does not have adverse effects. |
| • Define a post-war role for SME support programmes via detailed plans for adjustment and strengthened monitoring and evaluation mechanisms. |
| • Enhance the coverage of the credit register by broadening the scope of credit information sources. |

- Improve the functioning of enforcement mechanisms within the secured transactions framework.
- Strengthen non-bank financing by updating the legal framework for factoring and developing public support mechanisms to catalyse VC operations.
- Develop regulation for digital finance via a dedicated focal point within the NBU, more institutionalised coordination mechanisms, and measures to connect international peers.

**Supporting SME access to markets**

- Strengthen public procurement for SMEs by greater use of beneficial features like division into lots, and focus on long-term policy development, consolidating recent, positive changes, enhancing e-procurement, and improving procurement officials' skills.
- Prioritise SME familiarity with standards, basic training, and digitising public services, while addressing market surveillance gaps.
- Boost SME internationalisation by enhancing GVC integration, promoting e-commerce, and tackling trade facilitation gaps with regional peers.

**Fostering innovation and business support**

- Develop a new medium-term strategic framework for SME support services as soon as conditions allow.
- Monitor and enhance Diia.Business Support Centres to ensure outreach to rural SMEs.
- Consider introducing a dedicated programme for SME digitalisation
- Introduce grants for accessing private BDS providers and refine evaluation of support schemes.
- Implement measures to stimulate business innovation, adjust existing incentives for SMEs, and improve monitoring and evaluation of innovation policies.
- Adjust indirect incentives for innovation to match smaller-scale projects typical of the SME sector.
- Develop a strategic approach to support SMEs in the green economy, allocate funding for the National Action Plan, and establish dedicated financial support programmes for SME greening.
- Enhance access to green loans for SMEs and leverage donor-led initiatives for promoting green economy policies and bridging financing gaps.

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## Notes

[1] For more information on the analytical framework, please refer to the thematic chapter Digital Economy for SMEs.

[2] For more information on EU Directive 2019/1023, see https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019L1023.

[3] Diia.Business has a separate export education webpage containing 11 export-oriented courses – including Branding and Customer Experience, Marketing, Helping SMEs Generate Export Business, Public Procurement, Smart Exporter: Electronic Platforms, Regulations, and Export Requirement to the EU, among others.

[4] See: https://business.diia.gov.ua/social-entrepreneurship.

[5] "Ten steps to start your own business". See: https://business.diia.gov.ua/courses/10-krokiv-dla-pocatku-vlasnoi-spravi.

[6] The annual percentage rate (APR) provides the interest rate equivalent for a whole year, which helps borrowers with loan product comparisons.

[7] Agreement on Conformity Assessment and Acceptance of Industrial Products.

[8] See: https://eu-ua.kmu.gov.ua/sites/default/files/inline/files/vol_1._ch._i-viii.pdf.

[9] With the assistance of the Ministries of Digital Transformation and Foreign Affairs, see: https://odessa-journal.com/ukraines-businesses-launch-an-official-marketplace-to-promote-ukrainian-goods-abroad-and-support-the-countrys-recovering/

[10] See: https://neighbourhood-enlargement.ec.europa.eu/system/files/2023-02/SWD_2023_30_Ukraine.pdf, p. 16.

[11] See: https://zakon.rada.gov.ua/rada/show/v0285774-22#Text.

[12] Ukrainian Government (2021), СТРАТЕГІЯ інтеграції України до Єдиного цифрового ринку Європейського Союзу («Дорожня карта»), https://docs.google.com/document/d/1XgGb7AWSs7Ktl6Pl5xuYDpLFV0mtOTSN/edit#

[13] For information on the International Trade Council, see: https://tradecouncil.org/.

[14] https://export.gov.ua/

[15] The results of the assessments of different markets can be found at the following link: https://export.gov.ua/142-industrii.

[16] https://export.gov.ua/415-e-commerce

[17] The one-to-one consultations available through *Diia.Business* described above are one-off sessions with industry experts, offering their support on a voluntary basis.

[18] The survey highlighted that 1) Ukrainian businesses lack information about local R&D opportunities and do not fully understand the costs of R&D options, and 2) that the domestic scientific community is disproportionally focused on the needs of large businesses. Respondents to the survey also provided an indication of specific technologies needed to innovate in different sectors.

# Annex A. Methodology for the Small Business Act assessment

The SME Policy Index is a benchmarking tool for emerging economies to monitor and evaluate progress in policies that support SMEs. The tool is structured around the ten principles of the Small Business Act for Europe (SBA), providing a wide range of measures to guide the design and implementation of SME policies. The main objective of the SME Policy Index is to provide governments with a framework to assess policies targeting SME development. The Index identifies strengths and weaknesses in policy design, implementation, and monitoring, allows for comparison across countries and measures convergence towards EU SME policy standards. For more detailed information on the assessment framework and process, please refer to the chapter "Policy framework, structure of the report and assessment process".

Based on lessons learnt from previous SBA assessments and to capture important changes and emerging trends in the business and policy environment, this cycle benefitted from an updated assessment methodology, which broadened the scope of the analysis to cover new topics, such as policies for SME digitalisation and the responses to the COVID-19 crisis.

This annex provides a detailed explanation of the methodology used to calculate the 2024 SME Policy Index. In particular, i) it outlines the guiding principles of the methodology update, ii) it describes in detail the methodology used to calculate the 2024 scores, and iii) it presents the methodology used to calculate 2020 and 2024 comparable scores to safeguard comparability with the previous assessment.

## Revision of the scoring methodology

### *Guiding principles for the revision of the methodology*

The OECD has undertaken a revision of the methodology used to calculate the SME Policy Index, guided by four key principles to enhance its effectiveness and relevance.

1. Firstly, in order to **reduce the response burden on respondents**, the OECD carried out a comprehensive revision of the questionnaire through which the information used for the computation of the index scores is gathered. Ambiguous questions are clarified, and duplications or obsolete items are removed to streamline the data collection process. Additionally, for the first time, the questionnaire has been delivered using an online platform to improve the overall user experience, ensuring greater efficiency and accessibility.
2. Secondly, the revised methodology seeks to **capture emerging economic and policy trends and priorities**. Numerous factors contribute to keeping the business environment in a constant state of flux, including technological advancements, globalisation, shifts in consumer behaviour, evolving regulatory landscapes, and unexpected crises. To capture this changing environment, new questions have been added to the questionnaire, encompassing crucial areas, including responses to the COVID-19 crisis and digitalisation. Digital technologies have spread rapidly in recent years and found new applications in many dimensions of our societies, and the COVID-19 pandemic has further accelerated these trends. Digital adoption offers SMEs a clear opportunity to introduce fundamental changes to the way they do business, experiment with new technologies and

ultimately increase productivity. To achieve this, policy makers should adopt a comprehensive approach to designing and implementing policies for SME digitalisation (OECD, 2021[1]; OECD, 2021[2]). Government support to SME digitalisation has been chosen as the thematic focus of this edition of the SME Policy Index as the OECD identifies it as a strategic policy priority to modernise EaP economies, increase overall productivity, and bridge the productivity gap between SMEs and larger firms. In particular, the updated methodology underpinning this edition of the SME Policy Index aims to incorporate the progress made by EaP governments to support the digital transformation of SMEs as part of its broader assessment. To capture these policy efforts, the updated methodology includes a dedicated pillar on Digital Economy framework conditions, and six additional digitalisation-oriented sub-dimensions incorporated into the five core assessment pillars (see Box A A.1 for a list of the new digitalisation-oriented sub-dimensions).

3. Thirdly, the revised assessment methodology **strengthens the link between policies and outcomes**. This involves considering countries' ability to regularly collect statistical information about outcome-oriented key performance indicators, thereby providing the evidence base for more robust assessments of policy effectiveness.
4. Lastly, while introducing these improvements, the new SME Policy Index strives to **safeguard comparability with previous SBA assessments**. Consistency in assessment allows for tracking progress over time and facilitates comparisons between different evaluation cycles.

By following these guiding principles, the revised methodology for the SME Policy Index aims to provide governments with a more effective and reliable framework to assess policies supporting SME development and to foster convergence towards EU SME policy standards.

### Box A A.1. Digitalisation-oriented sub-dimensions introduced to the 2024 SBA assessment questionnaire

Five digitalisation-oriented sub-dimensions have been added to already existing dimensions of the SBA assessment. In particular:

- In the dimension *Institutional and Regulatory Framework for SME Policy*, the new sub-dimension ***Institutional Settings for SME Digitalisation*** analyses whether and how support to SME digitalisation is embedded in the framework for SME policy making.
- In the dimension *Access to Finance*, the new sub-dimension ***Digital Financial Services*** investigates the development of regulatory and supervisory frameworks for digital financial services.
- In the dimension *Standards and Technical Regulations*, the new sub-dimension ***Digitalisation of Standards and Technical Regulation*** evaluates support and training offered to SMEs on standards and technical regulations for their integration into the EU Digital Single Market; the digitalisation of processes within authorities responsible for technical regulation, national standards and accreditation bodies, metrology institutes, and market surveillance authorities; and the introduction by accreditation bodies, Conformity Assessment Bodies (CABs), and surveillance authorities of remote audit and inspection activities.
- In the dimension *Business Development Services*, the new sub-dimension ***Business Support Services for the Digital Transformation of SMEs*** looks at government-led initiatives to support the digital transformation of SMEs. These may include informational support, trainings, financial instruments and advisory services to better understand company needs, procure digital technologies, and develop tailored digital roadmaps.

In addition to these new sub-dimensions, the new pillar ***Digital Economy Framework Conditions*** assesses the state of framework conditions for SME digitalisation in EaP countries, looking at:

- Overall policy framework – national digital strategy or equivalent.
- Broadband connectivity,
- Digital skills.

Besides these newly introduced elements, a number of sub-dimensions already included in previous assessments also cover issues related to digitalisation. These include ***E-government services*** and ***Use of e-commerce***.

The *Digital Economy Framework Conditions* pillar and the mentioned digitalisation-oriented sub-dimensions have been averaged to obtain a composite score for SME digitalisation policies capturing cross-cutting policy efforts to promote digitalisation among SMEs.

### *Process followed to reach consensus on the new methodology*

To gather feedback and endorse the updated SME Policy Index methodology, the OECD organised three dedicated online workshops to present the new methodological approach with key stakeholders. These included government representatives of EaP countries, in particular the SBA co-ordinators, as well as representatives from other international organisations, such as the EU, EBRD, ETF, and UNECE. The revised questionnaire was shared in advance of each meeting to facilitate the discussion.

The three workshops took place in spring 2022:

- On 30 May 2022 the OECD presented the guiding principles of the methodology update and described in detail the amendments to Pillar A (Responsive government) and Pillar B (Entrepreneurial human capital).
- On 14 June 2022 the discussion focused on changes affecting Pillar C (Access to finance) and Pillar D (Access to markets).
- On 21 June 2022 the conversation revolved around updates to Pillar E (Innovation and business support) and a new area of assessment covering Digital economy framework conditions.

## Scoring methodology

The SME Policy Index is calculated through a process articulated in subsequent phases.

### *Data collection, evaluation, and verification*

The information that feeds into the 2024 SME Policy Index is collected through a questionnaire containing about 1 000 questions, grouped by policy dimension and in turn organised in sub-dimensions. In addition, for each dimension a set of outcome-oriented indicators is collected to strengthen the link between policies and outcomes (see above). In turn, each sub-dimension includes a number of thematic blocks, each with their own set of questions. These thematic blocks are typically broken down into the three components or stages of the policy process (design, implementation, monitoring and evaluation).

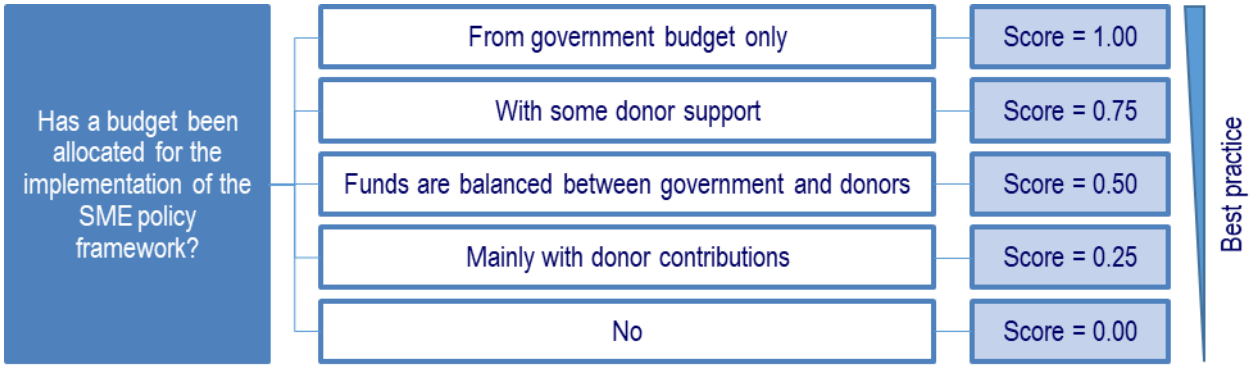
This approach allows for better monitoring of policy progress and enhances the depth of policy recommendations, while addressing systemic policy issues in a more detailed manner. Each block contains two types of questions: 1) core questions to determine the assessment score; and 2) open questions to acquire further descriptive evidence. Core questions have a defined set of answer options.

The SBA assessment questionnaire is sent to appointed government representatives (the “SBA co-ordinators) in each EaP countries. Through this questionnaire, national governments carry out a self-assessment of their policy frameworks. In parallel, the OECD and its partners conduct an independent assessment via extensive desk research and follow-up with relevant stakeholders in order to fill information gaps and resolve inconsistencies in findings. This process is essential to ensure that questions have been correctly interpreted and that the answers are consistent across countries and, where relevant, over time. To facilitate the verification process, the questionnaire asks national authorities to provide evidence in support of the responses provided to each question. The assessment also benefits from inputs by a team of local experts.

### *From qualitative information to quantitative values*

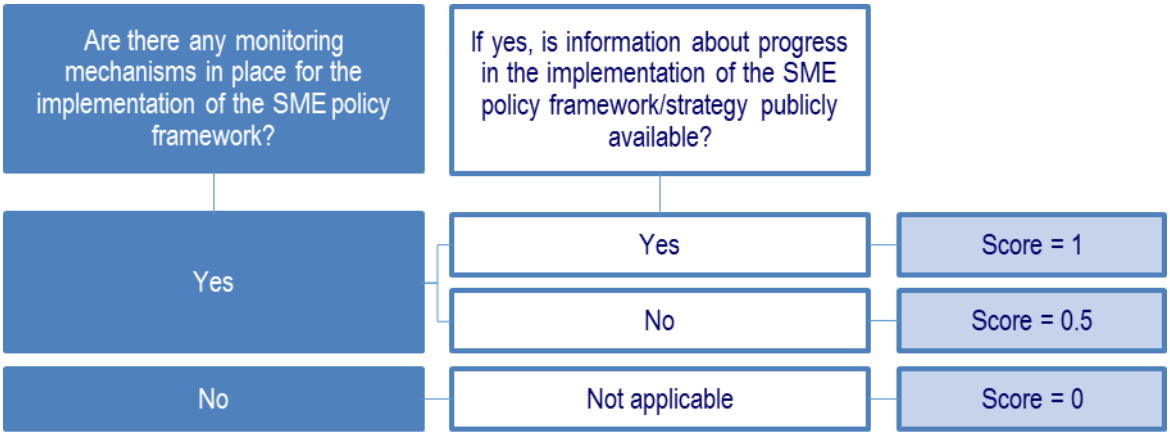
The qualitative information collected through the core questions of the questionnaire is converted into quantitative values. Each answer option provided to a core question is assigned a score from 0 to 1 where 1 represents alignment with best practice (see Figure A A.1).

### Figure A A.1. Example of scoring of a core question




Sometimes the answers to two or more questions can be scored jointly. An example can be seen in Figure A A.2 and relates to the two questions: "Are there monitoring mechanisms in place for the implementation of SME policy framework?", and "If yes, is information about progress in the implementation of the SME policy framework/strategy publicly available?". In this case, the scores are attributed to a combination of the answers to the two questions and the two questions represent a so called data point.

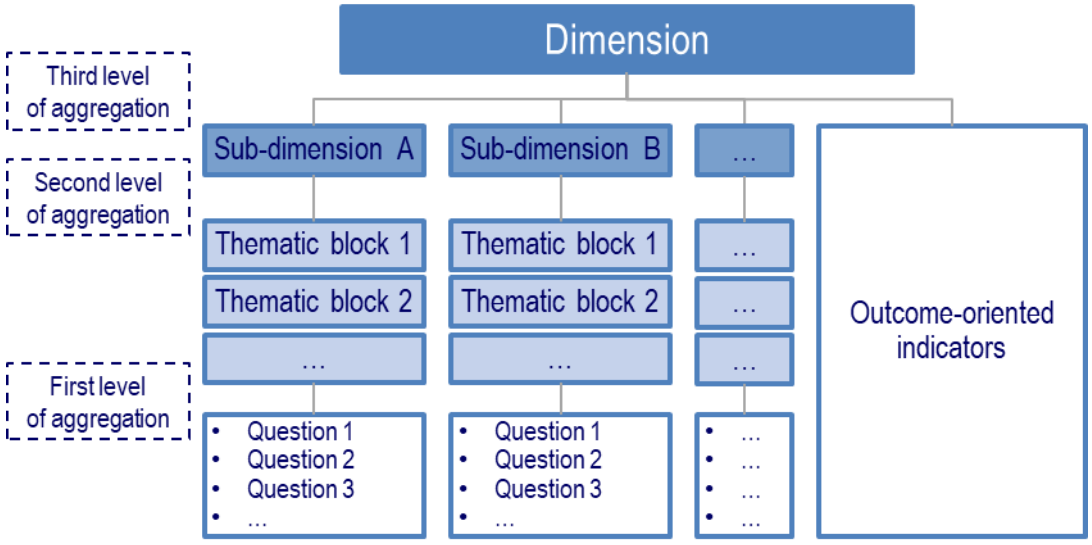
### Figure A A.2. Example of a score attributed to a combination of the answers




#### *Final SME policy index scores*

Once 0-1 scores are assigned to the core questions, a weighted average is computed to obtain scores at thematic block level. The obtained scores are then converted into the 1-5 scale. Scores for the thematic blocks are then aggregated to attain a score for the sub-dimension, with each component being assigned a weight based on expert consultation. The final step to obtain the overall 1-5 dimension score requires the aggregation of the sub-dimensions scores as well as the score assessing countries ability to collect outcome-oriented indicators. The latter is calculated as the proportion of indicators that a country collects over the total of requested indicators. Sub-dimension scores and scores assessing the ability to collect outcome-oriented indicators are finally aggregated using expert-determined weightings (based on the relative significance of each policy area) to reach an overall 1-5 dimension score. Figure A A.3 presents the structure of the SME policy index and the different levels of aggregations to obtain the final scores at dimension level.

### Figure A A.3. Structure of the SME policy index

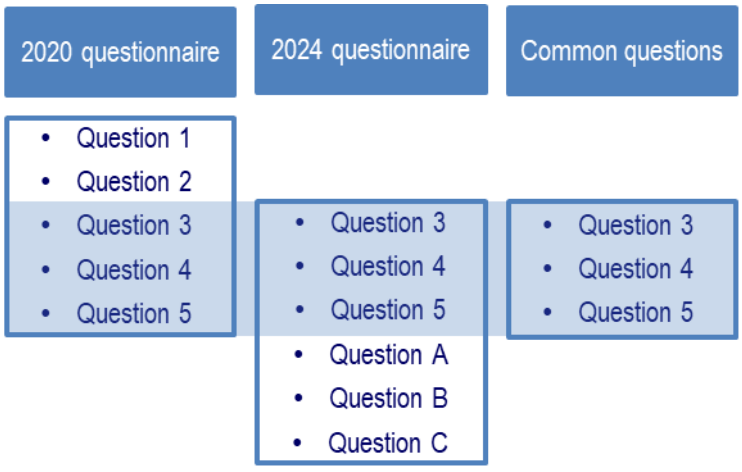



## Methodology to compute comparable scores

As described at the beginning of this annex, the 2024 assessment questionnaire has undergone a major revision. The differences in the 2024 SBA questionnaire and the 2020 SBA questionnaire imply that the scores as calculated and presented in this report and in the report published in 2020 (OECD et al., 2020[3]) are not immediately comparable. However, the OECD remains committed to safeguarding comparability with previous SBA assessments. To this end, both 2024 scores and 2020 scores have also been recalculated using a comparable methodology that allows to obtain an indication of the direction and magnitude of the policy changes.

While it is true that some new questions have been added and others have been removed, there is a bulk of questions that are common to both assessments. The 2024 and 2020 comparable scores have been calculated on the basis of the sub-set of questions common to both questionnaires (see Figure A A.4).

### Figure A A.4. Questions used to calculate comparable scores



Once identified the sub-set of common questions to the 2 SBA questionnaires, the responses provided in 2020 and in 2024 have been used to calculate comparable scores according to the same methodology described above.

## References

OECD (2021), *Beyond COVID-19 Advancing Digital Transformation in the Eastern Partner Countries*, OECD Publishing, https://www.oecd.org/eurasia/Beyond%20COVID-19%20Advancing%20Digital%20Transformation%20in%20the%20Eastern%20Partner%20Countries%20.pdf. [1]

OECD (2021), *The Digital Transformation of SMEs*, https://www.oecd-ilibrary.org/industry-and-services/the-digital-transformation-of-smes_bdb9256a-en. [2]

OECD et al. (2020), *SME Policy Index: Eastern Partner Countries 2020: Assessing the Implementation of the Small Business Act for Europe*, SME Policy Index, OECD Publishing, Paris/European Union, Brussels, https://doi.org/10.1787/8b45614b-en. [3]

SME Policy Index

# Eastern Partner Countries 2024

## BUILDING RESILIENCE IN CHALLENGING TIMES

The SME Policy Index: Eastern Partner Countries 2024 – Building resilience in challenging times is a unique benchmarking tool to assess and monitor progress in the design and implementation of SME policies against EU and international best practice. It embraces the priorities laid out in the European Union's SME Strategy for a sustainable and digital Europe and is structured around the ten principles of the Small Business Act for Europe, which provide a wide range of measures to guide the design and implementation of SME policies. This report marks the fourth edition in this series, following assessments in 2012, 2016, and 2020. It tracks progress made since 2020 and offers the latest key findings on SME development and related policies in the countries of the Eastern Partnership (EaP). It also identifies emerging challenges affecting SMEs in the region and provides recommendations to address them. The 2024 edition benefits from an updated methodology that also offers a deeper analysis of policies to support the digital transformation of SMEs.

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