SME Policy Index

Eastern Partner Countries 2012

PROGRESS IN THE IMPLEMENTATION OF THE SMALL BUSINESS ACT

OECD

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European Bank for Reconstruction and Development

SME Policy Index: Eastern Partner Countries 2012

PROGRESS IN THE IMPLEMENTATION
OF THE SMALL BUSINESS ACT
FOR EUROPE

OECD
BETTER POLICIES FOR BETTER LIVES
European Commission
ETF Working together Learning for life
European Bank for Reconstruction and Development

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Organisation profiles

Organisation for Economic Co-operation and Development (OECD), Eurasia Competitiveness Programme

The OECD Eurasia Competitiveness Programme, launched in 2008, helps accelerate economic reforms and improve the business climate to achieve sustainable economic growth and employment in two regions: Central Asia (Afghanistan, Kazakhstan, the Kyrgyz Republic, Mongolia, Tajikistan, Turkmenistan and Uzbekistan), and Eastern Europe and South Caucasus (Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine).

The programme works to improve the business climate through a comprehensive approach to evaluate policy, define priorities and support capacity building and implementation of reform. It achieves impact by helping countries align to OECD standards, such as the OECD Declaration on International Investment and Multinational Enterprises. It helps foster the implementation of OECD tools and instruments, such as the Policy Framework for Investment (PFI) and supports countries in the Eurasia region in conducting OECD flagship reviews in collaboration with respective Committees. OECD experts work closely with public authorities, the private sector and civil society to design and implement tools and instruments that lead to policy reforms and improve the business climate.

European Commission, Directorate-General for Enterprise and Industry

DG Enterprise and Industry is tasked with ensuring a well-run internal market for goods and promoting the competitiveness of EU enterprise, thereby making major contributions to the implementation of the Lisbon Growth and Jobs Strategy. DG Enterprise and Industry pays particular attention to the needs of manufacturing industries and small and medium-sized enterprises: it manages programmes to encourage entrepreneurship and innovation and ensures that Community legislation takes proper account of their concerns.

The DG Enterprise and Industry objectives are:

- To promote the European growth and jobs strategy.
- To strengthen the sustainable competitiveness of EU industry (industrial policy).
- To increase innovation.
- To encourage the growth of small and medium-sized enterprises.
- To make sure the single market for goods benefits EU industry and citizens.
- To strengthen the space sector and improve security technology.

DG Enterprise and Industry accomplishes its tasks in several ways. It has developed expertise in economic analysis. It manages regulation in the commercial sectors for which it is responsible. It has a budget to support specific actions. And it supports the continual scrutiny of member states' enterprise policies through the open method of co-ordination.

European Training Foundation

The European Training Foundation (ETF) is a specialised EU agency that supports 31 partner countries to harness the potential of their human capital through the reform of education, training and labour market systems in the context of the EU's external relations policy. The ETF's vision is to make vocational education and training in the partner countries a driver for lifelong learning and sustainable development, with a special focus on competitiveness and social cohesion.

The ETF's added-value comes from its neutral, non-commercial and unique established knowledge base consisting of expertise in human capital development and its links to employment. This includes expertise in adapting the approaches to human capital development in the EU to the context of the partner countries supporting the development of home-grown solutions.

European Bank for Reconstruction and Development

The EBRD is an international financial institution that supports projects from central Europe to central Asia. Investing primarily in private sector clients whose needs cannot be fully met by the market, the Bank fosters transition towards open and democratic market economies. In all its operations the EBRD follows the highest standards of corporate governance and sustainable development. Owned by 63 countries and two intergovernmental institutions, the EBRD maintains a close political dialogue with governments, authorities and representatives of civil society to promote its goals.

During 2011 the Bank responded to a call from its shareholders for an expansion of the mandate to include the southern and eastern Mediterranean (SEMED) region. This is part of the international community's support for the emerging Arab democracies. In 2012 the Bank will implement its expansion and initiate its investments in the SEMED region, subject to shareholders' ratification.

Eastern Partnership

This study is developed within the framework of the Eastern Partnership that was launched by the European Union in May 2009 in Prague. The Eastern Partnership has as main goal to create the conditions to accelerate political association and deepen economic integration between the EU and the six Eastern Partner countries – Armenia, Azerbaijan, Belarus, Georgia, Republic of Moldova and Ukraine.

At the political level, an Euronest Parliamentary Assembly was established to contribute to the strengthening, development and visibility of the Eastern Partnership, as the institution responsible for parliamentary consultation, supervision and monitoring.

Four thematic platforms of co-operation have been established, as the main tool of the Eastern Partnership multilateral work. SME development is one of the priorities under the Economic Platform. The purpose of the Eastern Partnership multilateral platforms is to familiarise the Eastern Partner countries with EU policies and working methods and identify directions for development in the region. Meetings are held at least twice a year at the level of senior officials engaged in the reform work in the relevant policy areas.

Panels and seminars organised under each platform address more in detail the subjects of the thematic platforms, with the participation of government officials with expertise in specific areas.

Foreword

Small and medium-sized enterprises (SME) are an important driver for job creation and economic growth. However, the global crisis has hit SMEs hard, restricting bank lending, eroding consumer demand, foreign direct investment, remittances and international capital inflows. To support SME development and stimulate growth, Eastern Partner governments from Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine are undergoing extensive reforms to enhance productivity, human capital and company level performance.

The SME Policy Index: Eastern Partner Countries 2012 – Progress in the Implementation of the Small Business Act for Europe *gives policymakers a framework to assess national SME policies. The report helps identify strengths and weaknesses in policy design and implementation, compare experiences and performance, set priorities and measure convergence towards implementation of the policy principles promoted by the Small Business Act for Europe.*

The report underscores the need for a more comprehensive approach towards SME development in the Eastern Partner region: reforms to improve the general business environment as well as targeted interventions to support SMEs. Wider policy reforms work to create a level playing field for SMEs through regulatory reform to cut back administrative burdens, investment in human capital and establishment of favourable framework conditions for access to finance. These policies should be complemented by specific mechanisms to support the internationalisation of SMEs, technology diffusion, entrepreneurship development and skills upgrading. Important sectors of Eastern Partner countries' economies such as agribusiness, information and communications technology, tourism and construction would benefit most from the recommended policy improvements.

By engaging government institutions and the private sector as well as non-governmental organisations, training providers and other stakeholders over a two-year period (2010-12), the assessment process generated new momentum to support SME development in the region. The assessment process benefited from similar exercises carried out in the Western Balkans in 2006, 2009 and 2012, and from the first assessment in the MEDA Region (EU Euro-Mediterranean Partner economies) conducted in 2008.

This publication is the result of a combined effort by the OECD, the European Commission, the European Training Foundation and the European Bank for Reconstruction and Development together with the national Small Business Act co-ordinators from the Eastern Partner countries. We look forward to continuing this close and fruitful co-operation on SME policies in favour of growth, jobs and social cohesion in the Eastern Partner region.

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This report is the outcome of work conducted by the six Eastern Partner countries (Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine), the OECD Eurasia Competitiveness Programme under the authority of the Eastern Europe and South Caucasus Initiative Steering Committee, the European Commission's Directorate-General for Enterprise and Industry (DG ENTR) within the framework of the SME Panel of the Eastern Partnership, the European Training Foundation (ETF) and the European Bank for Reconstruction and Development (EBRD).

The report was written under the guidance of Carolyn Ervin, Director for Financial and Enterprise Affairs (OECD DAF), Joanna Drake, Director for SMEs and Entrepreneurship and Chair of the SME Panel (European Commission, DG ENTR), John Farnell, former Director, and Didier Herbert, Director ad interim for Enterprise Competitiveness, Industry and Growth Policies (European Commission, DG ENTR), Madlen Serban, Director (ETF), and Erik Berglöf, Chief Economist, Special Counsellor to the President (EBRD), as well as Anthony O'Sullivan, Head of the Private Sector Development Division (OECD DAF), Fadi Farra, Head of the Eurasia Competitiveness Programme (OECD DAF), and Antonio Somma, Acting Head of the Eurasia Competitiveness Programme (OECD DAF), Christian Siebert, Head of International Affairs Unit (European Commission, DG ENTR), Arjen Vos, Head of Eastern Europe and Central Asia Unit (ETF), Andrew Kilpatrick, Director of Project and Sector Assessment (EBRD), and Jeromin Zettelmeyer, Deputy Chief Economist (EBRD).

Strategic oversight was provided by the Co-Chairs of the OECD Eastern Europe and South Caucasus Initiative, Poland (His Excellency Pawel Wojciechowski, Ambassador and Permanent Representative of the Republic of Poland to the OECD) and Sweden as well as by OECD Deputy Secretary-General Richard Boucher. The report benefitted from the financial support of the European Union and the Netherlands Embassy in Kyiv, Ukraine.

The work was led by Daniel Quadbeck (OECD DAF/PSD), Volker Genetzky (European Commission, DG ENTR), Olena Bekh (Specialist in Entrepreneurship and Enterprise Skills Development, ETF) and Anita Taci (EBRD), in co-operation with Marina Cernov (OECD DAF/PSD), Jibran Punthakey (OECD DAF/PSD), Anthony Gribben (Head of Enterprise and Entrepreneurship, ETF) and Beatriz Perez Timermans (EBRD). The report was developed under the supervision of Antonio Fanelli, Deputy Head of the OECD Private Sector Development Division.

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The methodology of this report benefitted from the experience of the Western Balkans and the Euro-Med region in which similar policy assessments were carried out in 2006, 2009 and 2012 jointly by the partner organisations. These reviews measure country convergence to the European Charter for Small Enterprises and, since 2008, to the Small Business Act for Europe.

In the Eastern Partner countries, the following SBA co-ordinators co-ordinated their countries' participation in all stages of the project: Aram Tshshmarityan (Armenia), Zaur Qasimov and Huseyn Pashayev (Azerbaijan), Tatsiana Laputskaya and Dmitry Kolkin (Belarus), Lali Gogoberidze (Georgia), Lilia Palii and Iulia Iabanji (Republic of Moldova), and Svitlana Svyshcheva and Olga Chernina (Ukraine). In particular, the SBA co-ordinators led the countries' self-assessment and co-ordinated the contributions of different government institutions and other national stakeholders.

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List of abbreviations

AB	Accreditation body
ACRA	Armenian Credit Reporting Agency
ADA	Armenian Development Agency
ADB	Asian Development Bank
AITT	Agency for Innovation and Technology Transfer, Republic of Moldova
ANFES	Azerbaijan National Fund for Entrepreneurship Support
ARMSTAT	Armenian Statistical Service of Republic of Armenia
ASRERS	Azerbaijan Real Estate State Register Service
AYEG	Association of Young Economists of Georgia
AZPROMO	Azerbaijan Export and Investment Promotion Agency
BAS	Business Advisory Services, EBRD
BAVIN	Business Angels and Venture Investors Network, Belarus
BBTC	Baku Business Training Center
BEEPS	Business Environment and Enterprise Performance Survey, EBRD
Belstat	National Statistical Committee of the Republic of Belarus
BIAC	Business and Industry Advisory Committee, OECD
BIPM	Bureau International des poids et mesures
BIZTAR	Business Regulatory and Tax Administration Reform Project, USAID
BSE	Baku Stock Exchange
BSP	Business service provider
BSTDB	Black Sea Trade and Development Bank
CBA	Central Bank of Armenia
CCI	Chamber of Commerce and Industry
CCR	Centralized Credit Registry
CEFE	Competency based Economies through Formation of Enterprise
CEN	European Committee for Standardisation
CENELEC	European Committee for Electrotechnical Standardization
CHB	Credit history bureau
CIG	Creditinfo Group Hf., Iceland
CIS	Commonwealth of Independent States
CMU	Cabinet of Ministers, Ukraine
CNPF	National Commission of Financial Market, Republic of Moldova
COOMET	Euro-Asian Cooperation of National Metrological Institutions
DCA	Development Credit Authority, Georgia
DCFTA	Deep and Comprehensive Free Trade Agreement
DG ENTR	Directorate-General for Enterprise and Industry
DVV	Institut für Internationale Zusammenarbeit des Deutschen Volkshochschul-Verbandes
EA	European Accreditation system
EAEC	Eurasian Economic Community

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EaP	Eastern Partner (country, region)
EBRD	European Bank for Reconstruction and Development, London, UK
EC	European Commission
EDRPOU	State Registry of Ukrainian Enterprises and Organizations
EEN	Enterprise Europe Network
EIF	Enterprise Incubator Foundation, Armenia
EIP	Entrepreneurship Indicators Programme, OECD-Eurostat
EITI	Extractive Industries Transparency Initiative, Azerbaijan
EIU	Economist Intelligence Unit
EL	Entrepreneurial learning
EMAS	EU Eco-Management and Audit Scheme
EMS	Environmental management standards
ENP	European Neighbourhood Policy
ETF	European Training Foundation, Turin, Italy
EU	European Union
FCBU	First Credit Bureau of Ukraine
FCG	Credit Guarantee Fund, Republic of Moldova
FDI	Foreign direct investment
FMO	Netherlands Development Finance Company
FTA	free trade agreement
GeoStat	Statistics Georgia
GEOSTM	Georgian National Agency for Standards, Technical Regulations and Metrology
GFPAA	Georgian Federation of Professional Accountants and Auditors
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
GNI	Gross national income
GNIA	Georgian National Investment Agency
GNSF	Georgian National Science Foundation
GRDF	Georgian Regional Development Fund
GRDF	Georgian Research and Development Foundation
GSE	Georgian Stock Exchange
GSP+	General Preferential Scheme for Sustainable Development
GTTC	Georgian Technology Transfer Center
ICT	Information and communication technology
IEC	International Electrotechnical Commission
IFC	International Finance Corporation
IFI	International financial institution
ILAC	International Laboratory Accreditation Cooperation
ILO	International Labour Organisation
IOLM	International Organization for Legal Metrology
IOM	International Organisation for Migration
ISCED	International Standard Classification of Education
KAB	Know About Business, ILO
KWF	*Kreditanstalt für Wiederaufbau*
LEED	Local Economic and Employment Development, Trento Centre, Italy
LL EL	Lifelong entrepreneurial learning
LTV	Loan-to-value (requirements for loans)
MENR	Ministry of Environment and Natural Resources, Azerbaijan
MES	Ministry of Education and Science, Armenia

MFI	Microfinance institution
MIEPO	Moldova Investment and Export Promotion Organisation
MIX	Microfinance Information eXchange
MoU	Memorandum of understanding
MSE	Moldova Stock Exchange
NAAU	National Accreditation Agency of Ukraine
NAPR	National Agency of Public Registry, Georgia
NASDAQ OMX	Nordic stock exchange
NBS	National Bureau of Statistics, Republic of Moldova
NCEQE	National Centre for Educational Quality Enhancement, Georgia
NGO	Non-governmental organisation
NPC	National Participation Council, Republic of Moldova
NQF	National Qualifications Framework
NVETC	National Vocational Education and Training Council, Georgia
ODIMM	Organization for SME Sector Development of the Republic of Moldova
PPC	Public-private consultation
PPL	Public Procurement Law, Azerbaijan
PPP	Public-private partnerships
QA	Quality Assurance
R&D	Research and development
RIA	Regulatory impact analysis
SAKPATENTI	National Intellectual Property Center, Georgia
SBA	Small Business Act for Europe
SCST	State Committee on Science and Technology, Belarus
SCURPE	State Committee of Ukraine for Regulatory Policy and Entrepreneurship
SEAF	Small Enterprise Assistance Funds
SEECEL	South East European Centre for Entrepreneurial Learning
SLA	Savings and loan association
SME	Small and medium enterprises
SME DNC	National Centre for SME Development of Republic of Armenia
SOFAZ	State Oil Fund of Azerbaijan
SPS	Sanitary and phytosanitary standards
SSRPE	State Service for Regulatory Policy and Entrepreneurship
STEP	Science and Technology Entrepreneurship Programme
TAM	TurnAround Management, EBRD
TNA	Training needs analysis
ToT	Training of trainers
TVET	Technical and vocational education and training
UFES	Ukrainian Fund for Entrepreneurship Support
Ukreximbank	State Export-Import Bank of Ukraine
UKRSTAT	State Statistics Service of Ukraine
UNCTAD	United Nations Conference on Trade and Development
UNESCO	United Nations Education, Scientific and Cultural Organisation
UNEVOC	United Nations Centre for Vocational education and Training
VET	Vocational education and training
WB	World Bank
WBCSD	World Business Council for Sustainable Development
WEE	Women's economic empowerment
WTO	World Trade Organisation

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Executive summary

The six Eastern Partner (EaP) countries (Armenia, Azerbaijan, Belarus, Georgia, Republic of Moldova and Ukraine) have emerged as an important economic region, strategically located between the East and West and in proximity to markets in the EU, the Middle East and Central Asia. With a combined total population of 75.5 million people, a highly educated workforce and vast land and energy resources, the region's average GDP growth reached 5.3% in 2010.

Nevertheless, the EaP region represents a group of heterogeneous countries which differ in terms of their geographical size, population, resource endowment and their stage of economic development. **Armenia, Georgia and the Republic of Moldova** are small, open economies with few resources and are highly dependent on agricultural production, the service sector and remittances. **Belarus and Ukraine** are rich in natural resources, particularly in mineral deposits, with a strong industrial base inherited from the Soviet Union, and high but volatile revenues from exports of commodities. Finally, **Azerbaijan** is an oil-based economy with about half of GDP stemming from industrial production in oil and gas extraction and related services, which have driven the country's economic growth for the last twenty years.

Despite these economic differences, small and medium-sized enterprises (SMEs) play an important role as key engines for further economic growth and employment in all EaP countries. In **Armenia, Georgia and the Republic of Moldova**, the SME sector represents an important part of the economy, accounting for a significant share of employment and providing a source of self-sustainable income. In **Belarus and Ukraine**, for many years SMEs played only a marginal role in the economy given the dominant position of large state-owned enterprises. New business opportunities for SMEs are likely to arise with further progress being achieved in privatisation and the establishment of functioning market economies. Similarly, in **Azerbaijan**, development of the SME sector has only recently become a priority for government policy as part of the country's efforts to diversify the economy and reduce dependence on the oil sector.

These factors explain why SMEs in the EaP countries today account for only about 50% of employment (compared to 60-70% in OECD economies) and contribute just over 30% to value added (in comparison to 55% in OECD economies). Nevertheless, policy makers across the region acknowledge that further expansion of the SME sector will be critical to sustaining high economic growth and employment generation for the young and rapidly expanding workforce.

OECD research shows that SMEs are an important driver of a country's competitiveness as they constitute a major source of knowledge, skills and innovation and contribute to employment generation and economic growth. Especially in a transition context such as in the EaP region, SMEs facilitate the shift from mass production to a demand-driven and

market-oriented supply of products. Moreover, SMEs compensate for unemployment related to the down-sizing of the public sector and are well positioned to quickly react to changing market conditions.

To leverage this potential and transform business opportunities for SMEs into economic growth, EaP countries will have to address a number of policy challenges that SMEs face due to their size, such as getting access to finance for SME growth, upgrading skills, or finding adequate business support services which are not delivered by the market. Government support in promoting SME development is necessary to find an appropriate response to address these challenges. Effective institutional structures and consultation mechanisms can help to overcome these constraints as small enterprises otherwise do not have the ability to influence nation-wide policies. SMEs in the EaP region would benefit from improved policy frameworks based on a coherent set of SME policies that foster entrepreneurship and competitiveness.

To support EaP countries in this effort, the *SME Policy Index: Eastern Partner Countries 2012* (Enterprise Policy Performance Assessment) has been jointly developed by the Organisation for Economic Co-operation and Development (OECD), the European Commission, the European Training Foundation (ETF) and the European Bank for Reconstruction and Development (EBRD) in collaboration with representatives from the Eastern Partner countries. It builds on the experience of the Western Balkans and the Euro-Med region where similar policy assessments were carried out in 2006, 2009 and 2012. For the first time, it also serves as a tool for policy makers from the EaP region to design and implement comprehensive tools and mechanisms to support SME growth and employment generation.

This report provides an assessment of the current status of SME policy development in all six EaP countries and gives a cross-country comparison, covering policy dimensions related to the ten principles of the Small Business Act for Europe (henceforth referred to as the EU Small Business Act). It assesses the strengths and weaknesses of SME policy frameworks currently in place in each of the EaP countries and provides recommendations on reform requirements for governments to address.

Key conclusions of the SME Policy Index 2012 for Eastern Partner countries

Most EaP countries have started to implement business climate reforms to create a conducive environment for private sector development; however, they still face significant challenges in developing a comprehensive approach towards the SME sector to complement these efforts.

EaP countries are supporting SMEs and entrepreneurship through business environment reforms

Creating favourable framework conditions for business operations should be one of the first priorities for policy makers. Horizontal policy reforms affecting the entire enterprise population in areas such as the operational environment for SMEs, legislative simplification and regulatory impact analysis (RIA) as well as legal and regulatory framework conditions for access to finance are an important precondition for entrepreneurial activities.

Overall, the assessment results show that EaP countries are taking a pro-active approach to streamline the operational environment for business activities. All EaP countries have simplified company registration procedures and it has become easier for companies to interact with public administrations through e-government services. In recent years, reforms to the company registration process have led to the removal of overly burdensome regulations, saving time and reducing costs for SMEs and entrepreneurs in general. In a number of cases (with the exception of Ukraine), countries have completely redesigned the registration process, by overhauling inefficient institutions and bringing administrative procedures in line with the world's most competitive standards. Starting a business in the region now takes between 2 days (Georgia) and 24 days (Ukraine) according to the World Bank's *Doing Business 2012* report.

All EaP countries have undergone reforms in legislative simplification, although some countries are more advanced than others. Georgia is most advanced in systematically reviewing and simplifying business-related legislation and applying legislative guillotine to redundant regulations. The country also shows the best results in a number of other fundamental policy areas that need to be addressed for the creation of a favourable business environment for companies of all sizes by establishing an efficient legal and regulatory framework for access to finance and public procurement policy. RIA, a policy tool to critically assess positive and negative effects of proposed and existing regulations, has already been implemented in Armenia and the Republic of Moldova and is about to be introduced in Georgia in the near future.

To support access to finance for SMEs, all EaP countries have started to improve the legal and regulatory framework to expand the financial sector beyond bank lending (*e.g.* microfinance, private risk capital), with mixed results. Private risk capital is scarce and equity markets are rather small and illiquid. As a result, bank lending remains the main source of external funding for SMEs but banks remain cautious about risk-taking. While cadastre and credit information systems are developed in Armenia and Georgia, and a unified collateral registry is in place in Georgia and the Republic of Moldova, enforcement of creditors' rights is generally weak across the region. An effective and easily accessible central collateral registry in Armenia, Azerbaijan and Belarus would be important for enhancing the legal and regulatory framework for SME financing.

Institutional framework for SME policy making to co-ordinate efforts is developing at different paces across EaP countries

A targeted approach towards the SME sector can complement reforms to the general business environment. Institutions and mechanisms for SME policy making are required to assess the need for policy interventions as a result of market failures and to co-ordinate those interventions to ensure that they are implemented effectively. EaP countries can be clustered into two groups in this regard.

The first group, including **Armenia, Georgia and the Republic of Moldova**, has started developing institutions and mechanisms for SME policy making through ongoing public-private consultations and effective policy co-ordination mechanisms. Armenia and the Republic of Moldova already have the main building blocks for SME policy in place, including an SME policy implementation agency and an SME strategy under development.

Both countries have begun to analyse and address policy constraints for SMEs in a comprehensive manner by moving towards the development of specific policy strategies with a focus on SME needs. Georgia has achieved noticeable results by following a horizontal approach to business climate development, based on effective institutions and mechanisms that serve the entire enterprise population.

As a next step, this group of countries would benefit from strengthening existing structures and improving the quality of the policy making process by assessing and addressing SME policy barriers in a more comprehensive manner. An analysis of country-specific SME sector needs and implementation of sector-specific SME policy tools would help those countries to strengthen SME competitiveness by, for example, addressing policy barriers in access to finance, enterprise skills, innovation and export-promotion.

The second group, including **Azerbaijan, Belarus and Ukraine**, has started providing support measures to the small business sector but this is often carried out in an *ad hoc* manner without a long-term plan in place and with only limited co-ordination between the relevant public authorities. All three countries implement pilot projects as a first response to perceived policy needs; however, they do not adequately assess market failures prior to an intervention. Also, responsibility for implementation of SME policy is not centralised in a single executive body. In Azerbaijan, a number of implementation agencies exist with a focus on different policy areas; however, co-ordination between those actors could be further increased to ensure a common approach towards the SME sector. In Belarus, SME policies are developed at the ministry level; however, no implementation body exists to transform policies into relevant programmes. In Ukraine, a new agency responsible for SME policy was established in March 2012, but its effectiveness will largely depend on a mandate and financing which have yet to be determined.

In these countries, official consultations with the private sector often have little impact on policy making and contain little representation on the part of SMEs. Consequently, stronger institutions in charge of SME policy development could encourage further development of the SME sector and guide public-private dialogue in this area. Particular focus should be given to strengthening institutions for SME policy making and increasing the level of participation of SMEs in the policy making process, by encouraging the development of transparent and inclusive SME associations that are actively involved in public-private consultations.

Targeted SME policy tools are required to further support SME growth across the region

Providing tailored support to SMEs and start-ups through SME policy tools can help to overcome policy challenges that persist in areas such as access to financial and human resources and participation of SMEs in export-oriented and innovative activities.

Support services for SMEs and start-ups (such as business incubators, consultancy services and financial support) are available across the EaP region as a combination of public and donor-funded programmes. In Armenia and the Republic of Moldova, support for SMEs and start-ups is envisaged in the draft national SME development strategies and extensive support programmes are delivered through their national SME support agencies. Advisory and financial support for start-ups is provided in Georgia and Ukraine through publicly funded schemes. Donor-funded business incubators have been set up in all countries, but

there is limited data on evaluating their effectiveness. Policy makers across the region need to ensure that SME support instruments such as business incubators and financial support schemes are only used in cases where the market fails to deliver the appropriate services.

Availability of financial resources remains a particular constraint to SME performance in all EaP countries. To support access to finance for SMEs, all EaP countries have started to develop specific instruments to encourage lending to SMEs (*e.g.* credit guarantee schemes, public start-up funding). Nevertheless, public support to SMEs is relatively weak and limited by fiscal constraints in most countries (apart from Azerbaijan). Even in countries where a number of good practices already exist, such as Armenia, Georgia and the Republic of Moldova, these instruments have had limited success given the impact of the credit crisis on the region and increased risk aversion of banks and other investors to lend to SMEs.

Promoting entrepreneurship needs to become a strategic objective of policy partnerships in all EaP countries, and requires a joint effort between major players of government, social partners and training providers. Countries like Georgia have started by introducing entrepreneurship education at individual levels of the education system, while Azerbaijan has made core skills development, including entrepreneurship, a centrepiece of the step-by-step reform of its national curriculum. Belarus has demonstrated a top-down drive by announcing a Year of Entrepreneurship, and now needs to make systematic efforts to bring the world of business and the world of education together. This may be achieved by following the example of the Republic of Moldova, which has brought all key stakeholders around the table to develop the human capital aspect of the SME support strategy. All countries have interesting practices at the level of schools and non-formal learning organisations, yet they should make more efforts to support good practice exchange and systemic policy dialogue for the development of "entrepreneurial ecosystems", as well as implementation of targeted support measures for women-led and women-owned enterprises. All EaP countries provide state-supported and private enterprise training through business support institutions; however, training is not always tailored to the needs of the small business community. Enterprises, in partnership with the public sector, will need to assume more responsibility for defining training needs and articulating these needs to the training market.

Policies to support export-oriented SMEs remain weak across the region, as most SMEs do not reach the necessary economies of scale to produce for international markets and build relevant networks. Given the relatively small size of their domestic markets (except Belarus and Ukraine), EaP countries have generally acknowledged the importance of exports for the growth of their firms. Armenia, Azerbaijan, Georgia and the Republic of Moldova have agencies that specialise in promoting their exporting firms. Developing export-led industrial strategies and identifying sectors in which EaP countries could have a competitive advantage would be an important next step.

Innovation policy tools remain inadequate in all EaP countries, with considerable scope for further development. In the wake of the recent global financial and economic crisis, well designed policy measures can be used to strengthen capacities of SMEs to absorb new technologies (*e.g.* through technology transfer centres). Financial support instruments could be further used to stimulate the development of partnerships between universities, SMEs and government financing to ensure innovation is market-oriented and driven by private sector demand (triple helix).

SME sector data remains scarce across the region

Even in those countries where policy formulation for SME support is already well advanced and sophisticated measures have been introduced, data on the SME sector remains scarce. Evidence-based policy making can only happen on the basis of accurate, up-to-date and detailed data, which allows policy makers to make an accurate assessment of the SME sector and come up with relevant and targeted solutions to existing problems.

The most comprehensive statistical websites with a large range of data on SMEs that is available online can be found in Georgia and the Republic of Moldova. Belarus collects a wide range of statistical data, however without publishing them online. In Armenia, Azerbaijan and Ukraine, official data on the SME sector is limited or fragmented across various sources. Having reliable statistical data on hand which also includes a breakdown of firms by sector would be an important condition for further improving targeted policy interventions.

Operational guidance for implementing SME-friendly policy reforms

There is no one-size-fits-all solution for advancing SME policy development across the region. All EaP countries are at different stages of economic development and heterogeneous with regard to their size, structure and resource endowment. Every EaP country has to find its own way to foster SME competitiveness and develop a country-specific approach adapted to the local economic context and structural challenges of the respective SME sector, taking into account the specific competitive advantages for SMEs and their market opportunities.

Nevertheless, all six EaP countries are invited to take advantage of the following operational guidance to structure their policy reform agenda to identify challenges and opportunities for SMEs and remove policy barriers limiting SME growth to create an enabling environment for SMEs:

- **Invite the private sector, and especially SME associations, to participate in regular consultations on business climate policy reform** to ensure that policy development is inclusive and meets private sector needs. Addressing the issue of business climate development in general would be an important first step. This could be complemented by focusing consultations on specific constraints faced by SMEs in key business sectors for SME growth. If appropriate, such consultations could lead to the development of comprehensive data-driven strategies and mechanisms to strengthen SME competitiveness by formulating an ambitious vision and well defined, measurable goals. Such a strategy needs to take into account the local economic context and prioritise policy measures that are instrumental to foster SME growth including entrepreneurial learning and enterprise skills, tools to facilitate access to finance for SMEs, export promotion and internationalisation, and business support services for innovative and high-growth SMEs. The experience of the Republic of Moldova shows that setting up an inclusive and constructive dialogue with the private sector and representatives from different government bodies can serve as a starting point for ongoing consultations and lead to effective policy reform.
- **Set up or further enhance the effectiveness of institutional structures to assess market failures and co-ordinate SME support measures** across ministries and agencies dealing with different aspects of SME development. As SME policy touches upon a wide range of

policy themes (finance, innovation, science, education, etc.), an increasing number of institutions are involved in the implementation of SME support measures. Given the complex nature of policy development and implementation, an effective co-ordination unit is required to ensure a common understanding of SME policy reforms and interventions among all stakeholders. Taking a comprehensive and well co-ordinated approach will ensure that SME policy elements are addressed as different components of a common system and not as individual policy areas under the sole responsibility of different ministries. Such a co-ordination unit may take the form of an inter-ministerial committee, or a specialised SME development department that has a mandate to liaise with all relevant ministries and government agencies.

- **Monitor and evaluate public policy tools on a regular basis to ensure policy tools are efficient and effective** in addressing market failures in areas such as access to finance, enterprise skills, innovation, business support services (*e.g.* training and consultancy services) and export promotion. SME policy tools can be used as an important instrument to support SME growth but policy makers need to ensure that public budgets are spent with care and that programmes do not create market distortions. Policy makers should make thorough assessments prior to any intervention in the market in support of the SME population and monitor programmes on an ongoing basis. EaP countries are invited to look at the OECD Framework for the evaluation of SMEs and entrepreneurship policies and particularly the "Six steps to heaven" methodology for assessing the impact of SME policy on companies.
- **Collect more detailed structural statistics and assess the performance of the SME sector** and the specific role SMEs play in their unique economic setting. This could be done by carrying out regular surveys on active companies with a needs analysis of SMEs by business sector to identify policy barriers that currently hinder SMEs from realising their full potential. Governments are encouraged to look into the Eurostat methodology for measuring entrepreneurship and the OECD Scoreboard on Financing SMEs and Entrepreneurs.

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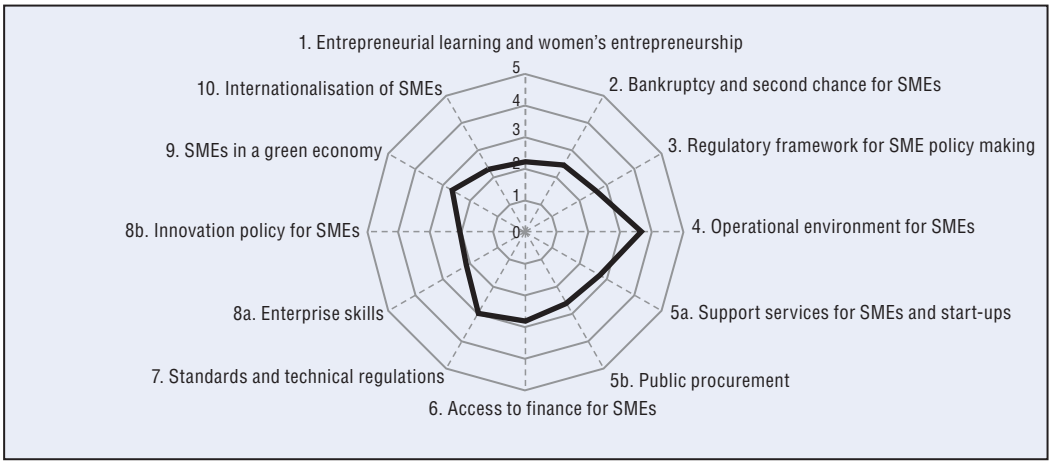
Key findings of the Small Business Act assessment

The following section provides an overview of key findings of the Small Business Act (SBA) assessment across twelve policy dimensions, based on ten SBA principles, at the regional and the country level. A detailed analysis and cross-country comparison by sub-dimension is presented in Part II of this report. Country profiles are provided in Part III.

Figure 1. **SBA results for Eastern Partner countries**



Notes: All policy dimensions are measured based on a set of relevant indicators with an SME focus.
All final scores have been calculated based on a set of weighted indicators relevant for SME policy development within each dimension (see Annex A). Indicators are structured around five levels of policy reform, with 1 being the weakest and 5 being the strongest. The policy development path for each indicator is typically structured as follows: Level 1: There is no framework (*e.g.* law, institution, project, initiative, etc.) in place to cover the area concerned; Level 2: There is a draft or pilot framework, and there are some signs of government activity to address the area concerned; Level 3: A solid framework is in place for this specific policy area; Level 4: Level 3 + some concrete indications of effective policy implementation of the framework; Level 5: Level 4 + some significant record of concrete and effective policy implementation of the framework. This level comes closest to good practices identified as a result of the EU Small Business Act and the OECD Bologna Process.

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Key findings per policy dimension

The following findings are the result of a collaborative policy assessment exercise carried out with the support of SBA co-ordinators in all Eastern Partner (EaP) countries. Assessment dimensions have been broken down into 92 indicators (see Annex A) which measure progress in policy development on a scale from one (low) to five (high). The scores presented in this section have been aggregated by policy dimension based on a weighted

average calculated according to the relative importance of each indicator (see scores and methodology section at the end of this chapter).

Dimension 1: Entrepreneurial learning and women's entrepreneurship

The first dimension considers how the various parts of the national administration in each country collaborate to strategically promote entrepreneurship across the learning system, together with the world of business and civic interest groups, with a particular focus on upper secondary education. Additional areas addressed are education and training for entrepreneurship outside the formal schooling system (*e.g.* NGOs and business support organisations) and how good practice is shared amongst the education and training communities. Second, the assessment considers how each country is addressing women's entrepreneurship.

On entrepreneurial learning, most countries have already engaged in multi-stakeholder policy dialogue to take forward the lifelong entrepreneurial learning agenda. However, this will require more concerted efforts in partnership building and committed leadership. While the assessment pointed to many interesting examples of good practice in all countries, particularly outside the formal education system, structured networks and exchange in the area were weak. Good efforts were noted on the promotion of entrepreneurship in upper secondary education. Nonetheless, more focused attention is necessary to ensure that entrepreneurship as a key competence is systematically addressed. On women's entrepreneurship, all countries have already taken a number of policy steps. These provide a good basis for a more developed engagement by the range of partners in the area. The report argues that women's entrepreneurship should be clearly embedded within the wider competitiveness drive in all countries.

In terms of next steps, the report recommends that the countries work together to develop entrepreneurship as a key competence, with specific reference to curriculum reform and teacher training, and make a particular effort to build networks to support policy advocacy for women's entrepreneurship, including training and mentoring services.

Table 1. **Weighted scores for dimension 1 for each EaP country and regional average**

Dimension 1	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	2.40	2.45	1.60	3.15	2.10	1.65	2.23

Dimension 2: Bankruptcy and second chance for SMEs

Dimension 2 addresses the need to implement well structured bankruptcy laws and to simplify bankruptcy procedures as an important condition for facilitating exit and re-entry of businesses into the market.

All EaP countries have laws and procedures on distressed companies, receivership and bankruptcy. However, the level of sophistication varies, especially with regard to commencement provisions, avoidance of pre-bankruptcy transactions and provisions relating to re-organisation proceedings which can be used among other indicators as a proxy to assess compliance of bankruptcy legislation and procedures with international standards. Bankruptcy proceedings are relatively streamlined in Armenia, Azerbaijan, Georgia and the Republic of Moldova. In Belarus, the average time spent in court procedures is excessively long (5.8 years); in Ukraine, procedures are very expensive and, on average, consume 42% of the estate's value.

In order to improve the efficiency of the process, reforms should be made to reduce delays. This would also have a positive effect on the cost of proceedings and the recovery rate. Measures may also be taken to ensure that bankruptcy cases are dealt with by specialised courts and that judges and officials in charge of administrating insolvency cases have received sufficient training. EaP countries would also benefit from formally regulating out-of-court settlement as an instrument to foster cost-effective management of insolvency processes.

Table 2. **Weighted scores for dimension 2 for each EaP country and regional average**

Dimension 2	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	3.17	2.50	2.11	2.94	2.53	1.94	2.53

Dimension 3: Regulatory framework for SME policy making

Dimension 3 measures progress in the development of an institutional framework for SME policy making including reforms in legislative simplification and effectiveness of public-private consultations.

In all EaP countries, institutions and mechanisms for SME policy making and public-private consultations are at an early stage of development. On the one hand, Armenia and the Republic of Moldova have the main building blocks for an SME policy in place, including an SME policy implementation agency and an SME strategy under development. Georgia has made significant achievements by following a horizontal approach to business climate development, based on effective consultations with the private sector and functioning intra-governmental co-ordination mechanisms. On the other hand, in Azerbaijan and Belarus, SME policy implementation is not centralised in one single body. In Ukraine, a new agency responsible for SME policy was established in March 2012, but its effectiveness will largely depend on its mandate and financing, which are yet to be determined. Also, official consultations with the private sector are limited, with little representation from SME associations. All EaP countries have undergone reforms in legislative simplification, although some countries (such as Georgia) are more advanced than others. Regulatory impact analysis (RIA) is implemented only in the Republic of Moldova and Armenia. The limited availability of internationally comparable and up-to-date statistical data on the small business sector remains a barrier to better policy making in all EaP countries.

In Armenia, Georgia and the Republic of Moldova more financing and strategic oversight is needed to make the institutional framework more efficient. Focus should be on strengthening the existing structures and improving the quality of the policy making process through regular consultations and RIA, as well as monitoring and evaluating existing programmes for SME support. In Azerbaijan, Belarus and Ukraine stronger institutions in charge of SME policy development could encourage further development of the SME sector and guide public-private dialogue in this area. Focus should also be on involving SME representatives from an early stage in the policy making process and encouraging the development of transparent and inclusive SME associations that have the capacity for active involvement in public-private dialogue. The collection and dissemination of more qualitative and up-to date statistical data should be considered by all EaP countries in order to improve the evidence base for policy making.

Table 3. **Weighted scores for dimension 3 for each EaP country and regional average**

Dimension 3	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	3.00	1.95	1.89	3.23	3.45	2.13	2.61

Dimension 4: Operational environment for SMEs

Dimension 4 assesses the extent to which public administrations have developed instruments to simplify regulations and reduce costs and procedures for SMEs. Examples of such measures include one-stop-shops for company registration and e-government solutions.

In recent years, EaP countries have made significant progress in reforming the operational environment for SMEs. In particular, reforms to the company registration process have led to the removal of overly burdensome regulations, saving time and reducing costs for SMEs and entrepreneurs. In a number of cases, countries have completely redesigned the registration process by overhauling inefficient institutions and bringing administrative procedures in line with the world's most competitive standards. In Georgia, the introduction of Public Service Halls has increased the accessibility of public services and reduced the administrative burden for SMEs by offering a broad range of services in a single location. Most EaP countries have streamlined their company registration procedures; however in Ukraine it can still take up to 24 days to complete the overall process. The introduction of e-government services in the EaP region has also led to a reduced administrative burden and greater accessibility of public services for SMEs. Countries have taken steps to develop a broad range of e-government services, often using online tax filing systems as a starting point. In addition, all EaP countries have introduced active measures to develop infrastructure for e-government through the introduction of legislation allowing for electronic signature.

In light of the significant progress that has been made so far, further reforms to the company registration process in the EaP region should focus on more advanced features such as online registration and increasing the effectiveness of one-stop-shops. In Azerbaijan, the Republic of Moldova and Ukraine, one-stop-shops currently do not allow for all necessary pre- and post-incorporation procedures to be completed in-house. Furthermore, the development of a broader range of functional e-government services such as social security returns, pensions, procurement and cadastre is needed in all EaP countries. Countries would also benefit greatly from the provision of a more effective and up-to-date infrastructure for e-government, by increasing connectivity between the databases of public administrations.

Table 4. **Weighted scores for dimension 4 for each EaP country and regional average**

Dimension 4	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	3.64	3.70	3.73	4.30	3.28	3.41	3.68

Dimension 5a: Support services for SMEs and start-ups

Dimension 5a measures the availability and accessibility of targeted support services for SMEs and start-ups. It also assesses the role of governments in identifying market failures in business service delivery and addressing those failures through public policy tools.

Information gaps and limited availability of business services for small firms are a common problem in all EaP countries. Governments respond to these challenges through various public policy tools to provide support services for SMEs and start-ups as a combination of public and donor-funded programmes. In Armenia and the Republic of Moldova, support for SMEs and start-ups is envisaged in the draft national SME development strategies and extensive support programmes are delivered through national SME support agencies. In both countries and in Georgia, the private market for business services is also relatively well developed. Advisory and financial support for start-ups is provided in Georgia and Ukraine via publicly funded schemes. In Azerbaijan, support services are provided through the national training centre. Donor-funded programmes (*e.g.* EBRD and the World Bank) are active in all countries in the region. Business information is widely available in all countries either through local information offices or online.

Overall, governments in EaP countries need to identify market failures to ensure that public money is used efficiently and that public support does not create market distortions or limit competition. International good practices should be imitated only with care, as every country's economic and policy environment is different, and SME needs may differ depending on this context. All EaP countries would benefit from developing mechanisms to assess the effectiveness of their SME and start-up support initiatives. For Azerbaijan, Georgia and Ukraine, creating a unified portal covering the entire spectrum of SME-related topics could significantly enhance the accessibility of the business community to information. The provision of public support services for start-ups could be considered in Azerbaijan and Belarus.

Table 5. **Weighted scores for dimension 5a for each EaP country and regional average**

Dimension 5a	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	3.28	2.12	2.41	2.92	3.79	1.77	2.71

Dimension 5b: Public procurement

Dimension 5b looks at policy mechanisms and tools that would encourage SMEs to participate in public procurement on an equal footing with larger companies.

Overall, progress differs among countries and significant divergences are visible on individual points. Most progress has been observed in providing publicly accessible information on public procurement tenders in all the countries. Further improvement is needed in the area of openness to foreign bidders, particularly in Belarus, where several restrictions are applied that limit access to public procurement by foreign companies. On the other hand, Belarus is the leader in cutting tenders into lots and setting proportionate qualifications and financial requirements for SMEs. Among EaP countries, only Georgia has implemented eProcurement. None of the EaP countries have developed a coherent policy framework to address late payments.

Countries are encouraged to move toward the EU public procurement standards, which in terms of transparency and non-discrimination can encourage a general amelioration of the public procurement environment, but also support SMEs by providing more information and transparency to the process of procurement. Simplification of procedures and the requirements for participating in procurement could be a first step to

giving SMEs better opportunities to participate in public procurement tenders, in particular in the Republic of Moldova. Even though some countries report that late payments are not a problem, this area definitely needs significant improvement. Allowing foreign firms to participate in the bidding process could also increase competition.

Table 6. **Weighted scores for dimension 5b for each EaP country and regional average**

Dimension 5b	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	2.14	2.29	3.14	4.14	1.43	2.57	2.62

Dimension 6: Access to finance for SMEs

Dimension 6 measures progress in access to finance for SMEs and in developing a legal and business environment supportive to timely payments in commercial transactions.

Despite improvements, in particular prior to the 2008 financial and economic crisis, access to finance for SMEs remains an important challenge for EaP countries. Bank lending, the main source of external funding for SMEs, has been significantly affected by the recent country-specific and international crises. Although there has been some recovery in credit growth in the region since 2010, banks remain cautious about risk taking. Other external sources of finance such as leasing are also affected by the crisis. They have yet to be developed as an alternative source of finance for SMEs. Private capital is scarce and equity markets are rather small and illiquid. Public support to SMEs is relatively weak and limited by fiscal constraints in most countries (apart from Azerbaijan). Progress in the development of the legal and regulatory framework is mixed across countries and indicators. While cadastre and credit information systems are developed in Armenia and Georgia, and unified collateral registry is in place in Georgia and the Republic of Moldova, enforcement of creditors' rights is generally weak across the region. Financial literacy remains low across the region but governments are recently becoming increasingly aware of this issue.

Enhancing competition and a greater level of sophistication in the banking sector would benefit SMEs in obtaining access to finance across the region. The funding model for many banks in the region remains a challenge, with a need to develop more local currency sources of funding and longer-term funding. General improvement of the business environment and corporate governance standards is necessary to increase investment opportunities and attract more private equity capital into the region. Building a domestic institutional investor base (*e.g.* through insurance and pension reform) and related exit opportunities would also help develop equity capital. Reducing the number of administrative procedures and regulations would increase the effectiveness of state financial support. An effective and easily accessible central collateral registry in Armenia, Azerbaijan and Belarus is important for enhancing access to finance for SMEs. The establishment of a private credit bureau in Azerbaijan and Belarus would benefit SMEs by improving information coverage and overcoming information asymmetries. The legal environment which protects creditors' rights by providing adequate enforcement mechanisms for the retrieval of collateral should be strengthened across the region. Increasing knowledge and general awareness of financial issues would also be beneficial to SMEs. For example, it could encourage SMEs to apply for a loan.

Table 7. **Weighted scores for dimension 6 for each EaP country and regional average**

Dimension 6	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	3.00	2.74	2.50	3.52	2.65	2.59	2.83

Dimension 7: Standards and technical regulations

Dimension 7 of the SBA is strongly related to the EaP trade agenda, as it aims to eliminate technical barriers to trade in the area of industrial and agricultural products. Technical barriers to trade can severely distort trade by preventing market access, protecting domestic producers and discriminating between domestic and foreign producers. As a number of EaP countries are granted tariff-free market access to the Single Market by benefiting from the special incentive arrangement for sustainable development and good governance (GSP+), today technical trade barriers represent one of the most important obstacles to the liberalisation of trade between the EU and the EaP countries.

Ukraine and Belarus are the best performing countries in the EaP region in addressing technical trade barriers for industrial products. The European Union (EU) completed negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA) between the EU and Ukraine in 2011, which implies already considerable approximation of legislation in the area of technical barriers to trade. In Belarus, the manufacturing sector has traditionally played a much more important role in economic activities than in other EaP countries. Furthermore, through the recently established customs union between the Russian Federation, Kazakhstan and Belarus, the quality infrastructure in Belarus is strongly aligned with the respective infrastructure of the Russian Federation. In the area of sanitary and phythosanitary rules, with the exception of Azerbaijan, the EaP countries have made considerable progress in aligning their legislation with the EU framework.

With the exception of the Republic of Moldova, all EaP countries are invited to further improve administrative and regulatory information for the business community, in particular for SMEs on how to comply with the legislative environment in the EU. It is positively acknowledged that various EaP countries (Armenia, Georgia, and the Republic of Moldova) have followed the example of Ukraine and started negotiations on a DCFTA with the EU. In the medium and long term this will lead to increased trade integration between the EU and the EaP countries and improved market access for EU companies and enterprises from the EaP countries.

Table 8. **Weighted scores for dimension 7 for each EaP country and regional average**

Dimension 7	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	2.38	2.13	3.75	2.88	3.38	3.25	2.96

Dimension 8a: Enterprise skills

Dimension 8a assesses human capital policy development measures and practices with regard to the SME sector and looks at the availability of training, its relevance to SME needs, the quality of training provided and its targeted character for both new and growing enterprises.

All countries in the region have policies, structures and resources allocated to SME training, available to various degrees, in the urban centres and in the regions and supported

by online tools. While the governments and social partners in Armenia, Azerbaijan, Georgia and the Republic of Moldova have established a dialogue to systematically assess the training needs of SMEs, actual practice in all six countries is mostly based on *ad hoc* individual efforts by training providers and employers. No country has an operational national quality assurance system, and the practice is limited to various cases of international accreditation of training courses, active use of various tools for evaluating the quality of training supply or the assessment of learning outcomes. Many countries of the region have already invested much effort in the development of quality standards of education and training provision, measures for national accreditation of providers or the development of National Qualifications Frameworks. Systemic implementation of policies and measures for ensuring quality, coverage and access of various target groups, including young entrepreneurs and women, to start-up training and support programmes, as well as services for growth enterprises is not yet available in the region, and the government SME statistics are too fragmented and incomplete to allow for effective monitoring of these efforts in all countries.

The countries need to address important elements of enterprise skills policies: the development of systemic mechanisms and tools for intelligence collection on the training needs of SME stakeholder and training-provider collaboration in strategic networks, focus on quality assurance systems and approaches and development of specific measures and institutional support structures for various types of enterprises including start-ups and growth enterprises. This requires a continued national policy dialogue among the main stakeholders following the SBA assessment process: the business community, training providers and government allowing partners to agree on how to ensure the availability of training and support services for SMEs, balanced across the territory of each country and covering the remote regions. The business community and the government must agree on the criteria for linking up training, advisory and financial support measures in all countries of the EaP region. Regular and systematic data collection on the training needs of small enterprises is an important part of an evidence-based policy monitoring culture.

Table 9. **Weighted scores for dimension 8a for each EaP country and regional average**

Dimension 8a	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	2.13	2.19	1.69	2.69	1.75	2.44	2.15

Dimension 8b: Innovation policy for SMEs

Dimension 8b provides a framework to analyse and evaluate policies that support innovation and technology transfer. The assessment focuses on the key elements needed to provide a favourable environment for innovative SMEs: institutional co-operation, the development of a strategic approach to innovation policy specific to SMEs, the establishment of innovation and technology centres and the development of a broad range of technical and financial support services.

In the EaP region, there is considerable scope for stimulating private sector involvement in innovation activities. In particular, innovation and technology transfer are constrained by top-down government interventions, non-transparent funding decisions, and a legacy of public R&D institutes that continue to operate in isolation from the private sector. Belarus and Ukraine are the best performing countries in the EaP region, as they

have developed the necessary institutional structure and documentation to support the development of innovation policy. However, innovation policy measures and programmes are not SME specific and too often remain on paper without sufficient financing attached. Also, state owned enterprises continue to be the primary beneficiaries of government support for innovation.

As a necessary first step, EaP countries should develop a strategic approach to the development of innovation policy, with active measures to support innovative SMEs and high-growth enterprises in various sectors of the economy. Innovation should feature as a core component of the policies of different departments and agencies, with efforts to avoid structural inefficiencies and encourage co-ordination of policy actions. In order to stimulate innovation and further encourage risk taking, EaP countries would benefit from targeted support services and financial instruments for innovative SMEs. These programmes can encourage greater private investment in R&D, address market failures constraining private investment, and reduce SMEs' reliance on donor-funded initiatives. The introduction of targeted measures to raise the absorption and innovation capacity of SMEs should be synchronised with the introduction of an incentive structure in the education and research area which bring the skills of workers, employees, managers and owners of SMEs on to a level with the production means, *i.e.* machinery and organisational innovation. Such an incentive structure would be conducive to trustworthy contract research, advice and other technical support services of public research with companies and the secondment of researchers to private companies.

Table 10. **Weighted scores for dimension 8b for each EaP country and regional average**

Dimension 8b	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	1.79	1.29	2.83	1.91	2.13	2.37	2.05

Dimension 9: SMEs in a green economy

Dimension 9 of the Small Business Act addresses the support of governments to SMEs so that they may benefit from green growth opportunities by adjusting their business models accordingly and the promotion of a policy framework towards eco-innovation and eco-efficient business.

With the exception of the Republic of Moldova, concepts of green economy, eco-efficient business and eco-innovation have been taken into consideration in the government policy frameworks of all the EaP countries. The business community is mainly informed on these issues by the government. In some of the countries, companies have been certified according to environmental management standards (EMS). Specific funding for SMEs for the promotion of eco-efficient business and the green economy is not available in any EaP country.

Given that green growth not only means a cleaner environment but also increased investment opportunities, it is recommended that countries move up green growth on their policy agendas, starting with the inclusion of green economy concepts in their respective SME programmes and strategies. This would encourage SMEs to invest in eco-efficient business and products and stimulate innovation towards environmentally friendly investments. The provision of information and programmes providing expertise could further enhance SME awareness about the benefits of green growth and implementation of EMS.

Table 11. **Weighted scores for dimension 9 for each EaP country and regional average**

Dimension 9	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	2.57	2.57	3.14	2.86	2.14	2.57	2.64

Dimension 10: Internationalisation of SMEs

Dimension 10 focuses on government support towards promoting export-oriented SMEs to access international markets.

All EaP countries have implemented programmes to encourage exports and, in the case of Azerbaijan, encouraging non-oil exports. Armenia, Azerbaijan, Georgia, and the Republic of Moldova have agencies that specialise in promoting export-oriented firms. However limited support is provided to SMEs. Armenia has created a link between the new Export-Led Industrial Strategy and the SME development strategy in order to support exporting SMEs in industry sectors. Neither Belarus nor Ukraine have specialised agencies, although they have developed state programmes for promoting exports.

Export promotion agencies in the EaP countries could further improve the capabilities of domestic SMEs to compete internationally by assisting them in obtaining good credit ratings, finding international partners, providing international market information, fostering research and development and implementing international quality standards. Creating greater awareness of export as a growth and market expansion opportunity can give a boost and increase the interest of firms in exporting. Finally, it is crucial that all export promotion activities of various government and non-government agencies are co-ordinated in order to avoid overlap and reach maximum efficiency. All countries should set up monitoring and evaluation mechanisms to make it easier to assess the effectiveness of export promotion programmes.

Table 12. **Weighted scores for dimension 10 for each EaP country and regional average**

Dimension 10	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine	EaP average
Weighted average	2.50	2.07	1.86	3.14	2.29	1.93	2.30

Assessment results by regional average

On a regional average, the assessment results can be sub-divided into three groups based on a simple regional average higher than 3, between 2.5 and 3 and lower than 2.5:

- A regional average **higher than 3** has only been achieved in Dimension 4 dealing with the operational environment for SMEs (regional average of 3.68). All six EaP countries score higher than 3 in this dimension showing that all EaP countries have implemented recognisable reforms to simplify administrative regulations, namely through streamlined company registration procedures and a number of e-government tools which help to reduce time and cost for SMEs in dealing with public administrations.
- A simple regional average **between 2.5 and 3** has been achieved in Dimensions 2 (bankruptcy and second chance, 2.53), 3 (regulatory framework for SME policy making, 2.61), 5a (support services for SMEs and start-ups, 2.71), 5b (public procurement,

2.62), 6 (access to finance, 2.83), 7 (standards and technical regulations, 2.96) and 9 (green economy, 2.64). Armenia, Georgia and the Republic of Moldova are outperforming their peers in Dimension 3 with a score of higher than 3, showing that these three countries have started to develop a comprehensive approach towards actively pursuing business climate reforms and promoting the SME sector. Armenia also has a score higher than 3 in Dimension 2; Armenia and the Republic of Moldova in Dimension 5a; Belarus and Georgia in Dimension 5b; Armenia and Georgia in Dimension 6. On the other hand, Belarus, the Republic of Moldova and Ukraine are stronger than their peers in Dimension 7 dealing with technical standards and regulations. Belarus is the only country in the region that achieves a score higher than three in Dimension 9 – supporting SMEs for a green economy.

- Finally, a simple regional average **lower than 2.5** has been achieved in Dimensions 1 (entrepreneurial learning and women's entrepreneurship 2.23), 8 (enterprise skills, 2.15 and innovation policy for SMEs, 2.05) and 10 (internationalisation, 2.30). These results indicate that there is still significant room for improvement across the region to develop and implement policies with a specific SME angle in those areas. Most countries might have started to consider developing a policy but not much progress has yet been achieved (with some exceptions, such as Georgia in Dimensions 1 and 10).

Key country findings

Armenia is a small, landlocked country and highly reliant on external flows of financing, in particular remittances stemming from its large international diaspora. The SME sector contributes considerably to Armenia's development and accounted for 42.5% of GDP and 42.2% of employment in 2009. SMEs mostly operate in trade, services and the construction sector. Given the high importance of SMEs for the Armenian economy, the government pursues a pro-active approach to supporting SME growth. Key developments over the past decade have been the establishment of an SME policy implementation agency, the creation of an SME Support Council, good efforts to promote entrepreneurship in secondary education and to implement trainings for start-ups, and, recently, work on a new SME strategy. Despite these improvements and the fact that the government has declared SME development as one of its strategic priorities, the sector is still in need of effective policy implementation mechanisms. According to SBA assessment, key areas which should be prioritised are SME financing, innovation and export promotion.

In **Azerbaijan**, industrial production in oil and gas extraction and related services represent more than half of GDP (52% in 2011, according to the Azerbaijan National Statistical Committee). There are limited opportunities for SMEs in this sector and most small businesses operate in low value-added sectors, such as wholesale and retail trade, agriculture and construction. Nevertheless, in recent years, Azerbaijan has made significant progress in acknowledging the key role of small business in the diversification of its economy and in setting up an institutional and legislative framework to start promoting entrepreneurship. The SBA assessment identified the improvement in the regulatory environment as one of Azerbaijan's key achievements, in particular its simplification of regulations to start a business by reducing the number of days required, procedures and costs. It has also introduced online registration for both individual entrepreneurs and legal entities. Nevertheless, much remains to be done in terms of strengthening intra-governmental co-ordination mechanisms, creating more opportunities for the small business sector to participate in the policy-making process through public-private consultations, and better representation of SME interests within

existing associations and other advocacy groups. Azerbaijan stands out for its policy effort to promote lifelong entrepreneurial learning particularly in compulsory education, while primary policy work to promote women's entrepreneurship provides a good basis for more strategic developments.

Belarus is the second largest economy in the EaP region. The economy is made up primarily of large industrial enterprises inherited by the state from the Soviet Union; large-scale privatisation has not yet started. State-owned enterprises generate about 70% of GDP and 50% of employment (Belstat). Consequently, statistics on SME performance show that the sector is highly underdeveloped. SMEs only contributed to about 20% of GDP and 28% of employment in 2010. The government has recently started to take a more proactive approach to supporting private entrepreneurship in Belarus. The value of private sector participation in the economy is increasingly acknowledged by the government and steps towards the development of a comprehensive SME support policy are underway. Nevertheless, the government remains cautious in implementing the more far-reaching economic reforms required to support SME growth. The announced liberalisation of economic activities should be promptly transformed into concrete actions since up to now the government continues to rely heavily on large, state-owned enterprises rather than creating truly level playing-field conditions for SMEs. Policy advocacy for women's entrepreneurship is weak, and the promotion of entrepreneurship through education, training and building policy partnerships with the private sector for entrepreneurship promotion will require more focused attention.

In **Georgia**, the SME sector represents a large share of the business population (96%), the majority of which consists of small enterprises (87.6%). Despite this figure and the strong economic growth of the Georgian economy, the SME sector still shows weak performance in terms of value added. In 2010, the SME sector in Georgia accounted for only 19.3% of value added and 16.1% of total turnover (GeoStat). Georgia has made significant progress in the area of improving the business environment for SMEs by simplifying administrative regulations, reducing the tax burden and fighting corruption. Georgia's economic policy reform agenda aims at creating a favourable business environment for all enterprises, irrespective of their size. Liberalising the conditions for doing business in Georgia has been achieved by simplifying regulatory practice, facilitating free trade, promoting privatisation campaigns, and creating policy partnerships for lifelong entrepreneurial learning. Georgia's SBA assessment reflects this approach and shows high scores for the operational environment and access to finance, while the key policy ingredients for more developed women's entrepreneurship are in place. While these improvements were an important first step, the country would benefit from pursuing a more targeted approach with a stronger focus on policy measures such as enterprise skills, innovation policy and SME support services. At present, SMEs do not play an important role on the economic policy agenda, given their small production value and turnover. A more pro-active approach towards SMEs in the areas of knowledge accumulation, capital investments and absorption capacities to benefit from modern technologies would help to unleash the economic growth potential within the SME sector.

The **Republic of Moldova** is a relatively small country, landlocked with limited natural resources apart from agricultural land. SMEs play an important role in this economic setting and contributed 28.3% to GDP in 2010. SME policy in the Republic of Moldova has been developing successfully over the past five years. The SBA assessment shows that there has been significant improvement in registration procedures and e-government. The

regulatory framework has been further simplified with the second stage of regulatory reform, the so-called Guillotine II and II+, but is not yet complete. A third stage, which tackles issuing of permits, started in 2011. While reforms in the area of a regulatory framework are ongoing, addressing the needs of businesses already operating remains a key issue. Public-private dialogue often does not involve representatives from the SME community, and could benefit from strengthening its formal influence on the decision-making process. Also, there has been limited support for the provision and improvement of the quality of business services. Formal and non-formal education and training do not match the type and level of skills that are demanded by SMEs, while greater efforts are needed to embed entrepreneurial learning across the education system, including teacher education. A national programme for gender equality provides a good basis to move forward with more focused support for women's entrepreneurship. The international donor community remains the main financial provider and supporter in this area. Access to finance also continues to be a crucial issue, particularly for SMEs.

Ukraine is the largest country in the EaP region. Industry and agriculture, the main export-oriented sectors of Ukraine's economy, represented 41.2% and 7.7% of GDP in 2010 respectively (Ukrstat). The contribution of SMEs to the economy has decreased over the past four years; employment decreased particularly in medium-sized enterprises, approximately 10% each year between 2007 and 2010. The SME sector currently accounts for 58.1% of total employment (small – 26.3%; medium – 31.8%). In terms of turnover, the share of the SME sector has dropped from 60.7% in 2007 to 51.2% in 2010. These downward trends across all main indicators suggest that the SME sector needs more enabling policies to foster SME competitiveness. The government has made a number of commitments to support SME development; however, there is little follow through to effective implementation of reform. The absence of a coherent approach to SME policy making and the lack of an efficient strategy, policy tools or resources, often leave the outlined directives on paper without implementation. Important initiatives in the areas of innovation policy, access to finance and SME support tools have been set, but most have not been enforced due to a lack of political will and/or insufficient funding. This is reflected in Ukraine's low score for the "think small first" principle. At the time of writing of this report, the country had no functioning government entity in charge of SME policy development or implementation. The institutional framework for SME policy making needs strengthening and should be complemented with an efficient mechanism for public-private dialogue and monitoring tools, and where women's entrepreneurship should have a dedicated support line. The assessment notes good efforts to promote entrepreneurship in secondary education while a broader policy support framework could prompt entrepreneurship more systemically across the learning system, with a specific focus on entrepreneurship competence. The country also scores low in the area of business service provision and export promotion of the SME sector.

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Scores and methodology

Small Business Act scores

The following table displays the Small Business Act (SBA) scores in the Eastern Partner (EaP) countries based on the SBA assessment. The cut-off date for the assessment process was 31 March 2012. The assessment framework is derived from the ten principles of the Small Business Act and further broken down into 12 policy dimensions, 20 sub-dimensions and 92 indicators. Each indicator is structured around five levels of policy reform, with 1 being the weakest and 5 being the strongest. For further details please see the methodology (next section).

Table 13. **Small Business Act scores**

Name of indicator		Scores							Weights
		ARM	AZE	BLR	GEO	MDA	UKR	EaP	
I)	***Create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded***								
1.	**Entrepreneurial learning and women's entrepreneurship**	**2.40**	**2.45**	**1.60**	**3.15**	**2.10**	**1.65**	**2.23**	
	Policy framework for entrepreneurial learning (EL)								
1.1.1.	Policy partnership	2	2	1	4	2	2		*3*
1.1.2.	Good practice exchange	1	1	1	3	1	1		*1*
1.1.3.	Non-formal learning	1.5	2	1.5	1.5	1	1		*1*
	Upper secondary education (ISCED 3)								
1.1.4.	ISCED 3 Entrepreneurial learning	4	4	3	3	2	2		*2*
	Women's entrepreneurship								
1.1.5.	Policy support framework for promotion of women's entrepreneurship	2.5	2.5	1.5	3	3	1.5		*3*
II)	***Ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance***								
2.	**Bankruptcy and second chance for SMEs**	**3.17**	**2.50**	**2.11**	**2.94**	**2.53**	**1.94**	**2.53**	
2.1.	**Bankruptcy procedures**	**4.00**	**3.25**	**2.00**	**3.00**	**3.13**	**2.00**		***2***
2.1.1.	Laws and procedures on distressed companies, receivership and bankruptcy	4	3	3	3	3.5	3		*1*
2.1.2.	Bankruptcy time (DB indicator)	4	3	1	2	3	3		*1*
2.1.3.	Cost (% of the estate) (DB indicator)	5	5	2	5	4	1		*1*
2.1.4.	Recovery rate (cents on the dollar) (DB indicator)	3	2	2	2	2	1		*1*
2.2.	**Second chance**	**1.50**	**1.00**	**2.33**	**2.83**	**1.33**	**1.83**		***1***
2.2.1.	Promoting positive attitude towards giving entrepreneurs a fresh start	1	1	1	1	1	1		*1*
2.2.2.	Discharge from bankruptcy	1	1	4	5	1	2		*1*
2.2.3.	Debt settlement	2.5	1	2	2.5	2	2.5		*1*

Table 13. **Small Business Act scores** *(cont.)*

Name of indicator		Scores							Weights
		ARM	AZE	BLR	GEO	MDA	UKR	EaP	
III)	***Design rules according to the "think small first" principle***								
3.	**Regulatory framework for SME policy making**	**3.00**	**1.95**	**1.89**	**3.23**	**3.45**	**2.13**	**2.61**	
3.1.	**Institutional framework**	**3.43**	**2.25**	**2.00**	**2.61**	**3.25**	**2.07**		***3***
3.1.1.	SME definition	5	2.5	3.5	3	5	4		*2*
3.1.2.	Availability of statistical data on SMEs	2	2	2.5	4.5	3	1.5		*1*
3.1.3.	Inter-governmental co-ordination in policy elaboration	3.5	3	3	3	3.5	2.5		*3*
3.1.4.	SME development strategy	2.5	2	1.5	2	2.5	1		*3*
3.1.5.	SME policy implementation agency or equivalent	4	2.5	1	1	3.5	2		*3*
3.1.6.	Measures to tackle the informal economy	3	1	1	4	2	1.5		*2*
3.2.	**Legislative simplification and regulatory impact analysis**	**2.85**	**1.60**	**1.45**	**3.55**	**4.05**	**2.35**		***2***
3.2.1.	Review and simplification of current legislation	4	2	1.5	5	4	3		*3*
3.2.2.	Legislative guillotine	3	2	1.5	4.5	4.5	2.5		*3*
3.2.3.	Use of regulatory impact analysis (RIA)	2	1	1.5	2	4	2		*3*
3.2.4.	The SME test	1.5	1	1	1	3	1		*1*
3.3.	**Public-Private Consultations (PPCs)**	**2.50**	**1.83**	**2.17**	**3.83**	**3.17**	**2.00**		***2***
3.3.1.	Frequency and transparency of public/private consultations (PPCs)	3	2	2	4.5	3.5	2		*1*
3.3.2.	Formal influence of PPCs	2	1.5	2	4	3	2		*1*
3.3.3.	Representativity of PPCs	2.5	2	2.5	3	3	2		*1*
IV)	***Make public administration responsive to SMEs***								
4.	**Operational environment for SMEs**	**3.64**	**3.70**	**3.73**	**4.30**	**3.28**	**3.41**	**3.68**	
4.1.	**Company registration**	**3.89**	**4.16**	**3.98**	**4.20**	**3.63**	**3.74**		
	Issuing of company registration certificate								***2***
4.1.1.	Number of days for obtaining a company registration certificate	4	3	4	5	4	3		*1*
4.1.2.	Number of administrative steps for obtaining a company registration certificate	4	4	4	5	4	4		*1*
4.1.3.	Official cost of obtaining the company registration certificate	4	5	4	3	4	4		*2*
	Company Identification Numbers								*1*
4.1.4.	Administrative identification numbers in dealing with the public administration	4	5	4	5	4	5		*1*
	Completion of the overall registration process and entry in operations								*1*
4.1.5.	Number of days for completing the overall registration process, including compulsory licenses for standard business activities (WB, *Cost of Doing Business Index*)	3	3	4	4	3	2		*1*
4.1.6.	Costs connected with registration (% of GNI per capita) – (WB, *Cost of Doing Business Index*)	3	3	4	3	2	3		*2*
4.1.7.	Minimal capital requirements (% of GNI per capita) – (WB, *Cost of Doing Business Index*)	5	5	5	5	4	4		*2*
	Advanced company registration process								*1*
4.1.8.	Progression to one-stop-shop (OSS)	4	4	5	5	4	4		*3*
4.1.9.	Online registration	4	3.5	2.5	2	2	1.5		*2*
4.1.10.	Silence-is-consent principle	2	2	1	5	3	3		*1*
4.2.	**Interaction with government services (e-government)**	**3.33**	**3.13**	**3.42**	**4.42**	**2.83**	**3.00**		
	E-government services								***2***
4.2.1.	Tax returns	4	4	4	5	4	4		*2*
4.2.2.	Social security returns	4	2	4	5	2	3		*2*
4.2.3.	Extension to other services (*i.e.* pensions, procurement, cadastre, etc.)	2	2.5	2	4	3	2		*1*
4.2.4.	Reporting on enterprise statistics	2	1	1	3	3	4		*1*
	E-government infrastructure								*3*
4.2.5.	Electronic signature (or equivalent)	4	4	4	4	3	3		*2*
4.2.6.	Connection between the databases of different public administrations, companies providing information only once, unless for updates	2	3	3	5	2	2		*1*

Table 13. **Small Business Act scores** *(cont.)*

Name of indicator		Scores							Weights
		ARM	AZE	BLR	GEO	MDA	UKR	EaP	
V)	***Adapt public policy tools to SME needs***								
5a.	**Support services for SMEs and start-ups**	**3.28**	**2.12**	**2.41**	**2.92**	**3.79**	**1.77**	**2.71**	
5a.1.	**SME support services**	**3.00**	**1.90**	**1.20**	**2.50**	**3.20**	**1.60**		***3***
5a.1.1.	Government action plan on business services	3	1.5	1	1.5	3	1		*3*
5a.1.2.	Range of business services	3	2.5	1.5	4	3.5	2.5		*2*
5a.2.	**Business information for SMEs**	**3.50**	**2.75**	**4.50**	**3.50**	**4.75**	**1.50**		***2***
5a.2.1.	Business information	4	2	5	5	5	2		*1*
5a.2.2.	Quality of online portal	3	3.5	4	2	4.5	1		*1*
5a.3.	**Support services for start-ups**	**3.67**	**1.50**	**1.83**	**3.00**	**3.67**	**1.00**		***1***
5a.3.1.	Business incubators	3	2	3.5	4	4	3.5		*1*
5a.3.2.	Advisory services support for start-ups	4	1.5	1	2.5	3	2.5		*1*
5a.3.3.	Financial services support for start-ups (vouchers, grants, etc.)	4	1	1	2.5	4	2.5		*1*
5b.	**Public procurement**	**2.14**	**2.29**	**3.14**	**4.14**	**1.43**	**2.57**	**2.62**	
5b.1.1.	Cutting tenders into lots	3	3	5	5	1	3.5		*1*
5b.1.2.	Information and publication of public procurement	4	4	5	5	3	4		*1*
5b.1.3.	Penetration of eProcurement	1	2	1	5	1	1		*1*
5b.1.4.	Ensuring that payments are made on time	1	1	1	2	1	1		*1*
5b.1.5.	Openness to foreign enterprises, either SMEs or large	4	1	3	5	2	5		*1*
5b.1.6.	Setting proportionate qualification levels and financial requirements	1	4	4	3	1	1		*1*
5b.1.7.	Allowing SMEs to bid jointly, *i.e.* to rely on the economic and financial standing and technical ability of other undertakings	1	1	3	4	1	2.5		*1*
VI)	***Facilitate SME access to finance and develop a legal framework and business environment supportive of timely payments in commercial transactions***								
6.	**Access to finance for SMEs**	**3.00**	**2.74**	**2.50**	**3.52**	**2.65**	**2.59**	**2.83**	
6.1.	**Sources of external finance for SMEs**	**2.29**	**2.50**	**2.36**	**2.64**	**2.43**	**2.50**		
6.1.1.	Credit guarantee schemes	3	2.5	2	2	3	3		*1*
6.1.2.	Public start-up funding	2.5	2.5	2	2	3	1		*1*
6.1.3.	Business angels network	1	1	2.5	2.5	1	1		*1*
6.1.4.	Microfinance facilities (including credit unions)	3	4	2.5	4	3	3		*1*
6.1.5.	Leasing	2.5	3	3.5	3	3	3.5		*1*
6.1.6.	Availability of risk capital (*e.g.* venture capital, private equity funds)	2	2.5	2	3	2	3		*1*
6.1.7.	Access to stock market	2	2	2	2	2	3		*1*
6.2.	**Legal and regulatory framework**	**3.40**	**2.90**	**2.60**	**4.00**	**2.80**	**2.60**		
6.2.1.	Cadastre	4	3.5	3.5	4.5	4	3		*3*
6.2.2.	Credit information services	5	3.5	2	4.5	2	3		*3*
6.2.3.	Registration systems for moveable assets	3	2.5	3	5	4	3.5		*3*
6.2.4.	Collateral and provisioning requirements	3	2	2.5	3	2	2		*3*
6.2.5.	Creditor rights	2	3	2	3	2	1.5		*3*
6.3.	**Other factors that affect demand and supply of finance**	**2.00**	**2.00**	**2.00**	**2.50**	**2.00**	**3.00**		
6.3.1.	Financial literacy	2	2	2	2.5	2	3		*1*
VII)	***Help SMEs to benefit more from the opportunities offered by the Single Market***								
7.	**Standards and technical regulations**	**2.38**	**2.13**	**3.75**	**2.88**	**3.38**	**3.25**	**2.96**	
7.1.1.	Technical regulations	2	2	3	3	3	3		*1*
7.1.2.	Standardisation	2	2	3	3	2	2		*1*
7.1.3.	Accreditation	2	2	3	3	3	4		*1*
7.1.4.	Conformity assessment	2	2	4	2	4	3		*1*
7.1.5.	Metrology	2	2	5	3	3	4		*1*
7.1.6.	Market surveillance	2	2	5	2	3	4		*1*
7.1.7.	Administrative and regulatory information	3	2	3	3	5	2		*1*
7.1.8.	Sanitary and phytosanitary standards (SPS) – institutional framework	4	3	4	4	4	4		*1*

Table 13. **Small Business Act scores** *(cont.)*

Name of indicator		Scores							Weights
		ARM	AZE	BLR	GEO	MDA	UKR	EaP	
VIII)	***Promote the upgrading of skills and all forms of innovation***								
8a.	**Enterprise skills**	**2.13**	**2.19**	**1.69**	**2.69**	**1.75**	**2.44**	**2.15**	
8a.1.1.	Training needs analysis (TNA)	2	2	1	2	2	2		*3*
8a.1.2.	Access to training	2.5	3.5	2.5	3.5	2	2.5		*1*
8a.1.3.	Quality assurance	2	2	2	3.5	1	3.5		*2*
8a.1.4.	Start-ups	2	2	2	2	2	2		*1*
8a.1.5.	Enterprise growth	2.5	2	2	3	2	2		*1*
8b.	**Innovation policy for SMEs**	**1.79**	**1.29**	**2.83**	**1.91**	**2.13**	**2.37**	**2.05**	
	Policy framework for innovation								***3***
8b.1.1.	Delegation of competencies and tasks	1	1	3	1.5	2	3		*2*
8b.1.2.	Strategic approach to broad innovation policy	2	1	3	2	2	2		*3*
	Support services for innovative companies								*2*
8b.1.3.	Establishment of innovation and technology centres	2	2	2	2	2	2		*1*
8b.1.4.	Innovation support services	2	1	2	2	2	2		*2*
8b.1.5.	Financial support services	2	2	3	2	2.5	2.5		*3*
IX)	***Enable SMEs to turn environmental changes into opportunities***								
9.	**SMEs in a green economy**	**2.57**	**2.57**	**3.14**	**2.86**	**2.14**	**2.57**	**2.64**	
9.1.1.	The "greening" of the current strategies in the field of SMEs, industry and innovation	2	2	2	2	2	2		*3*
9.1.2.	Availability of expertise to SMEs on environmental issues	3	3	4	4	3.5	3		*2*
9.1.3.	Promoting the use of environmental management systems and standards	3	3	4	3	1	3		*2*
X)	***Encourage and support SMEs to benefit from growth markets***								
10.	**Internationalisation of SMEs**	**2.50**	**2.07**	**1.86**	**3.14**	**2.29**	**1.93**	**2.30**	
10.1.1.	Export promotion programmes	2.5	3	2	3	2.5	2		*3*
10.1.2.	Financial support for export promotion activities	3	1	1.5	3	1.5	2		*3*
10.1.3.	National SME promotion events	1	2.5	2.5	4	4	1.5		*1*

Note: Indicators are structured around five levels of policy reform, with 1 being the weakest and 5 being the strongest. For further information please see the methodology.
Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Methodology

The *SME Policy Index* is a set of indicators that measure progress in the implementation of SME policy based on the principles of the EU Small Business Act. It also measures the level of convergence of the SME policy conducted by each of the EaP countries to the policy standards and good practices promoted by the EU and the OECD. The index allows comparing performances across the countries by transforming qualitative information into quantitative indicators. At country level it can be used as an instrument to identify strong and weak points as well as synergies and inconsistencies in policy development.

The index has been developed by the OECD Private Sector Development Division, in collaboration with the European Commission (DG Enterprise), the European Training Foundation and the EBRD. The index has already successfully been applied in other regions of the European Neighbourhood Policy (ENP), namely the Western Balkans and Turkey and the Middle East and North Africa. The original methodology has been adapted to the EaP context, following two regional workshops involving the country SBA co-ordinators.

Small Business Act assessment framework

The *SME Policy Index* indicators are derived from the ten principles of the EU Small Business Act listed in Table 14. Each principle has been broken down into policy dimensions and sub-dimensions that capture the critical feature of policy development in each specific area relevant for EaP countries. Specifically, the following dimensions and sub-dimensions have been assessed:

Table 14. **SBA principles, policy dimensions and sub-dimensions**

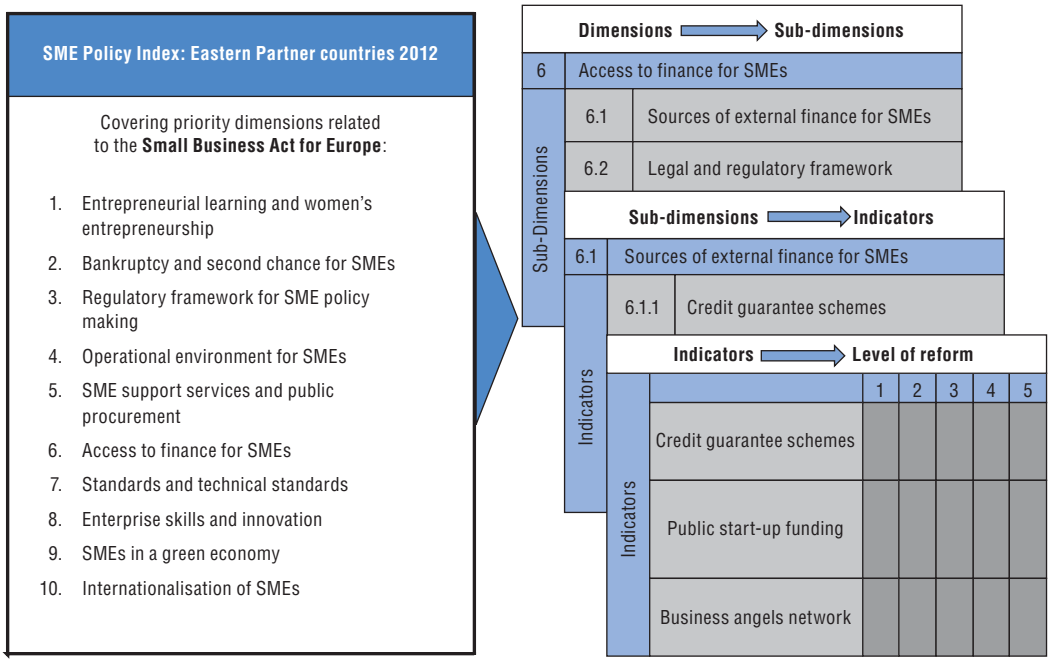
SBA principle	Policy dimension	Sub-dimension
I) Create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded	1. Entrepreneurial learning and women's entrepreneurship	● Policy framework for entrepreneurial learning. ● Upper secondary education (ISCED 3). ● Women's entrepreneurship.
II) Ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance	2. Bankruptcy and second chance for SMEs	● Bankruptcy procedures. ● Second chance.
III) Design rules according to the "think small first" principle	3. Regulatory framework for SME policy making	● Institutional framework for SME policy development. ● Legislative simplification and regulatory impact analysis. ● Public-private consultations (PPCs).
IV) Make public administrations responsive to SMEs' needs	4. Operational environment for SMEs	● Company registration. ● Interaction with government services (e-government).
V) Adapt public policy tools to SME needs	5a. Support services for SMEs and start-ups	● SME support services. ● Business information for SMEs. ● Support services for start-ups.
	5b. Public procurement	● Public procurement.
VI) 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	● Sources of external finance for SMEs. ● Legal and regulatory framework. ● Other factors that affect demand and supply of finance.
VII) Help SMEs to benefit more from the opportunities offered by the Single Market	7. Standards and technical regulations	● Standards and technical regulations.
VIII) Promote the upgrading of skills in SMEs and all forms of innovation	8a. Enterprise skills	● Enterprise skills.
	8b. Innovation policy for SMEs	● Policy framework for innovation. ● Support services for innovative companies.
IX) Enable SMEs to turn environmental changes into opportunities.	9. SMEs in a green economy	● Green economy.
X) Encourage and support SMEs to benefit from the growth markets.	10. Internationalisation of SMEs	● Export promotion.

Sub-dimensions have then been further broken down into 92 measurable policy indicators which are structured around five levels of policy development, with 1 being the weakest and 5 being the strongest (see Annex A for further information).

Allocation of scores

There are two types of indicators: quantitative and qualitative. The quantitative indicators give a score based on the value of a certain figure. For example, most of the indicators from Dimension 4 (Operational environment) are based on specific indicators such as the number of days for obtaining a company registration certificate or the number of administrative identification numbers in dealing with the public administration.

Figure 2. **Assessment framework based on the EU Small Business Act**



Qualitative indicators give a score based on the level of policy development in a certain area and transform qualitative information into quantitative indicators to measure progress in reform implementation. The policy development path of qualitative indicators is typically structured along the following lines:

- **Level 1:** There is no framework (*e.g.* law, institution, project, initiative) in place to cover the area concerned.
- **Level 2:** There is a draft or pilot framework and there are some signs of government activity to address the area concerned.
- **Level 3:** A solid framework is in place for this specific policy area.
- **Level 4:** Level 3 + some concrete indications of effective policy implementation of the framework.
- **Level 5:** Level 4 + some significant record of concrete and effective policy implementation of the framework. This level comes closest to good practices as identified by OECD standards.

To provide an example of a qualitative indicator, Table 15 shows the measurement for indicator 6.1.1 (credit guarantee schemes), which is a part of sub-Dimension 6.1 (Sources of external finance for SMEs), Dimension 6 (Access to finance for SMEs), based on SBA principle VI (Facilitate SME access to finance and develop a legal and business environment supportive of timely payments in commercial transactions).

A score of 4 or 5 is provided to countries that have privately operated credit guarantee facilities in place either funded by the state or through fees. However, countries that have one or several credit guarantee schemes in place that are established and controlled by the government receive a score of 3. A score of 2 is given if a scheme is under consideration. Finally, a score of 1 is given to countries that do not have any credit guarantee facilities and are not planning to have one.

Table 15. **Example of indicator**

		Level 1	Level 2	Level 3	Level 4	Level 5
6.	**Access to finance for SMEs**					
6.1.	**Sources of external finance for SMEs**					
6.1.1.	**Credit guarantee schemes**	No credit guarantee scheme in place.	Credit guarantee scheme facility under consideration.	Credit guarantee facilities in place. (government initiative and state controlled).	Credit guarantee facility operating under contract to the private sector but state-funded.	Number of mutual or mixed credit guarantee schemes in place under private managers able to finance themselves out of fees alone.

Weighting system

In order to create aggregated scores for each dimension, each indicator, and in some cases each sub-dimension, is allocated a certain weight according to its relative importance within a dimension. The weights are assigned through a process of expert consultation.

The highest weight of 3 is typically given to so-called driver indicators, which set the basis for policy development across a dimension. Secondary indicators, which typically measure the existence and sophistication of additional policy instruments, are given a weight of 2 or 1. An example of a driver indicator is the "policy partnership" indicator in Dimension 1 on entrepreneurial learning and women's entrepreneurship. Policy partnership measures the coherence between developments in entrepreneurial learning and wider policies in the country, and therefore is a fundamental condition for more specific entrepreneurial learning tools to be effective. Other examples of driver indicators are the indicators in sub-Dimension 6.2 on access to finance which measure the legal and regulatory framework for SME financing.

The weighted average is calculated as the sum of individual scores weighted with the share of the allocated weight in the total sum of weights for the dimension (or sub-dimension). The aggregation is done up to the level of dimensions, as they represent distinct policy areas.

The assessment process

The scores assigned to each indicator are the result of a process that is both participative and analytical. In order to reduce bias and mis-measurements in assigning a score to each indicator, the *SME Policy Index* approach is to conduct two assessments in parallel based on the same assessment grid. The first assessment is provided by the government as a self evaluation of the SME policy framework. It includes inputs collected from the different agencies and ministries involved in SME policy development and implementation under the responsibility of the country SBA co-ordinator, an SME policy senior official.

In parallel to the government self-assessment, an independent assessment is carried out by the OECD and the international and multilateral partner organisations. The independent assessment is based on inputs from a team of local experts that collect data and information and conduct interviews with key stakeholders and, in particular, with private sector representatives and business associations.

The country score for each indicator is the result of a consolidation of these two assessments, enriched with further desk research by the four partner organisations and additional inputs received through interviews and public-private reconciliation meetings including government officials and private sector representatives to ensure consensus on the scoring.

PART I

Overview of Eastern Partner countries and the SBA assessment process

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PART I

Chapter 1

Economic overview and the role of small and medium-sized enterprises in the Eastern Partner countries

The Eastern Partner (EaP) countries are heterogeneous in their size, population, resource endowment and their stage of economic and institutional development. This diverse group was strongly affected by the 2008-09 crisis in several ways: through external demand (particularly in the EU and the Russian Federation), terms of trade adjustment (Belarus and Ukraine) and the decline of remittances and FDI (Armenia, Georgia and the Republic of Moldova). After a period of growth until the end of 2011, the pace of recovery from the effects of the crisis has slowed in response to the deteriorating external environment and, in several countries, unfavourable domestic factors. The region's vulnerabilities remain significant due to its reliance on external demand to support growth, terms of trade pressures and the volatility of remittances.

Introduction

The Eastern Partner (EaP) region is composed of a group of heterogeneous countries in terms of their size, population, resource endowment and their stage of economic and institutional development. With a population of 75.5 million people (WB, 2012) the region has strong economic potential which is based on its strategic location between Europe, Asia and the Middle East, placing it in close proximity to considerable markets totalling over 400 million people (OECD, 2011a), vast land and energy resources, a relatively highly educated population and growing labour force and a strong record of foreign direct investment (FDI) inflows growing annually at over 10% between 2002 and 2008 (WB, 2012). In 2009, however, the financial crisis impacted GDP growth, and investment inflows into most countries of the region have decreased (OECD, 2011a). In 2010 the region's average GDP growth reached 5.3%,[1] while the aggregated GDP of the EaP countries is more than USD 270 billion (WB, 2012), which accounts for approximately 8.9% of the GDP of the wider (Eastern) Europe and Central Asia region (as defined by the World Bank).

A heterogeneous region with a diverse economic structure

The six EaP countries are very different in both population and size. Ukraine is by far the largest EaP country and stretches over about 60% of the region's territory; it also accounts for about 60% of the region's population. All five other countries have a population of less than 10 million each and are relatively small in size. The exception is Belarus which is less densely populated and accounts for almost one fifth of the region's territory – as much as Armenia, Azerbaijan, Georgia and the Republic of Moldova together.

Table 1.1. **Population and size in Eastern Partner countries, 2010**

	Population	Area
Armenia	3.1 million	29 740 sq. km
Azerbaijan	9.2 million[1]	86 600 sq. km
Belarus	9.5 million	207 600 sq. km
Georgia	4.5 million	69 700 sq. km
Republic of Moldova	3.6 million	33 850 sq. km
Ukraine	45.9 million	603 550 sq. km

1. Data based on national official sources.
Source: World Bank (2012), *World Development Indicators Database*, World Bank.

All six EaP countries have middle-income economies according to the World Bank classification based on gross national income (GNI). Armenia, Georgia, the Republic of Moldova and Ukraine are lower-middle income economies with a GNI per capita of up to USD 3 975. Azerbaijan and Belarus are considered higher-middle income economies with a GNI per capita of USD 5 330 and USD 5 950, respectively (in 2010).

With an average employment rate of 53%, which is lower than the OECD average at 56%, unemployment rates are high, ranging from 6% in Azerbaijan and the Republic of

Moldova to 29% in Armenia (data for Belarus are not available) (WB, 2012).[2] A large part of the population is informally employed, especially in the agricultural sector. At the same time, EaP countries experience significant outflows of skilled labour, especially in Armenia, Georgia, as well as in the Republic of Moldova, where the stock of emigrants represents approximately ¼ of the population (WB, 2011).

In terms of geographic location, Georgia and Ukraine have open access to international sea trade routes through the Black Sea. Armenia, Azerbaijan, Belarus and the Republic of Moldova are landlocked or with access to only a closed sea such as the Caspian Sea (Azerbaijan). As exporting companies from these countries face higher transport costs, potential export products are less competitive on the international market (UNCTAD, 2010). Nevertheless, all countries are linked to the surrounding regions by a network of railways and land routes, as well as a number of international airports. Due to their geographical position as a link between Europe and Asia, these countries also serve as important transit routes.

The European Union (EU) has common borders with Belarus, the Republic of Moldova and Ukraine. All EaP countries (except Belarus) signed a Partnership and Co-operation Agreement with the EU in the 1990s and are currently negotiating Association Agreements, which will bring them politically and economically closer to the EU.[3]

All six EaP countries are relatively open to trade. At the regional level, the Russian Federation and the EU are the main trading partners. The Russian Federation is the main import and export trade partner for all countries except Georgia and Azerbaijan. In the case of Belarus, in 2010 imports and exports reached 40% and 52% of GDP respectively. More than 50% of Azerbaijan's exports (mostly oil) go to EU markets, while imports stem largely from the Russian Federation and Turkey. Georgia exports mainly to its neighbours, with Azerbaijan, Turkey and Armenia as main export markets (40% of GDP in 2010) (EIU).

Azerbaijan, Belarus and Ukraine are resource-rich economies, with significant revenues from the export of commodities and the largest share of export to GDP (more than 50%). The exports of Azerbaijan are dominated by petroleum, which accounts for 94% of its total exports. About half of its GDP stems from industrial production in oil and gas extraction and related services. Belarus exports mineral products (28%) and chemicals and rubber (20%). Ukraine's economy is based on processing raw materials and exporting low-value-added products, such as non-precious metals (28.4% of exports in 2010), in particular steel and mineral products. In 2009, Ukraine was also the seventh largest exporter of wheat in the world (FAOSTAT). Both countries also export machinery and equipment (19% and 18% respectively) (EIU).

Armenia, Georgia and the Republic of Moldova are small economies that are highly dependent on services, agriculture and remittances (OECD, 2011a). Armenian exports are dominated by mineral products and base metals. In Georgia, GDP stems mainly from its services as a trade and transport hub. This is partly due to the country's geographical position as a transit corridor.

Land and energy resources are unevenly distributed across the region. The total agricultural area in 2009 accounted for 62 million hectares (FAOSTAT). Most of the agricultural land (67%) is in Ukraine. The country's proximity to the Black Sea guarantees a mild climate and allows Ukraine to grow winter and spring crops. Agricultural production is an important sector in all countries of the region, especially in Armenia and the Republic of Moldova where it accounted for 20% and 14% of value added in 2010 (compared to the regional weighted average of 8.5%).

Box 1.1. **Economic structure of EaP countries**

Armenia is a small country and is highly reliable on external flows of financing, in particular remittances stemming from its large international diaspora. In 2007-10 remittances accounted for approximately 9.5% of GDP (counting only remittances through official channels included in the balance of payments) (WB, 2012).* GDP growth is relatively low (2% on average in 2007-10) (WB, 2012) and the economy is still highly reliant on the agricultural and construction sectors; in 2010 each of these sectors represented 17% of GDP (EIU). Other important sectors of the economy are the extraction and processing of metals and ores, which represent 53% of total merchandise exports, as well as trade and catering (WB, 2012).

In **Azerbaijan**, industrial production in oil and gas extraction and related services represent more than half of GDP (52% of GDP in 2011 according to the Azerbaijan National Statistical Committee). During the financial crisis, the high reliance of the economy on oil exports represented a buffer against the crisis, allowing a high growth of 10% over 2008-09 (WB, 2012). On the other hand, oil dependence impoverishes businesses outside the oil sector as they then must operate in an environment with an appreciated currency, leading to cost pressures on domestic producers from cheap imports and lower competitiveness of domestic goods on external markets.

In **Belarus**, the economy is dominated by large state-owned enterprises, which generate approximately 70% of GDP and 50% of employment. Industry and manufacturing in particular are the main sectors of the economy, representing 65% and 31% of value added in GDP respectively (WB, 2012), the highest figure in the EaP region. A large share of its industrial products is exported to Commonwealth of Independent States (CIS) countries, and in particular to its partners in the Eurasian Customs Union, the Russian Federation and Kazakhstan. Due to its geographical position as a transit route, transport and communication services also represent an important source of its GDP and services exports.

Georgia's main economic activities include the cultivation of agricultural products such as grapes, citrus fruits and hazelnuts; mining; and the output of a small industrial sector which produces alcoholic and non-alcoholic beverages, prepared foodstuffs and chemicals. As an important transit corridor in the region, transport represents a significant part of Georgia's economy and services exports (51% in 2010) (WB, 2012).

The economic performance of the **Republic of Moldova** is modest. With a GDP per capita of USD 1 631, it is the lowest in the EaP region. As in the case of Armenia, the economy of the Republic of Moldova is reliant on large inflows of remittances from abroad (28% of GDP on average in 2007-10), which partly fuel its economic growth (WB, 2012). The Republic of Moldova exports mainly basic agricultural goods to CIS countries and manufactured products to the EU.

Ukraine is the largest economy in the EaP region, accounting for 45% of the regional GDP. Industry and agriculture are the main export-oriented sectors of the Ukrainian economy and represent 41.2% and 7.7% of GDP respectively (UKRSTAT). Services remain the largest sector, accounting for 45.8% of GDP (UKRSTAT). However, the economy is concentrated on processing raw materials rather than developing high-value-added finished goods. Exports are also low-value-added non-precious metals (28.4% of exports in 2010), in particular steel and mineral products (13.1%) (UKRSTAT). In 2009, Ukraine was also the seventh largest exporter of wheat in the world (FAOSTAT).

* Average 2007-10, counting only remittances through official channels, included in the balance of payments.

Macroeconomic environment affected by the crisis

The diverse group of EaP countries was strongly affected by the 2008-09 crisis through several channels: external demand (particularly in the EU and the Russian Federation), terms of trade adjustment (Belarus and Ukraine) and the decline of remittances and FDI (Armenia, Georgia and the Republic of Moldova). After a dip in early 2009, Azerbaijan's commodity-based economy continued to grow vigorously in 2009 following the rebound of hydrocarbon prices. Elsewhere, however, the downturns were quite severe, particularly in Armenia and Ukraine, where GDP fell by 14.1% and 14.8% respectively.

After growing strongly up to the end of the third quarter of 2011, the pace of the region's recovery from the effects of the crisis has slowed down in response to the deteriorating external environment and, in several countries, unfavourable domestic factors. Ukraine has suffered from lower external demand and tightening financial conditions. The growth of Azerbaijan's oil sector and economic activity in Belarus has slowed down as the authorities have tightened monetary and fiscal policies to contain the country's policy-induced balance-of-payments crisis. The economies of Armenia, Georgia and the Republic of Moldova have demonstrated some resilience so far, in part due to their lower level of integration into the European market.

The region experienced another period of inflation as global food commodity prices increased in late 2010. However, inflation has subsided more as food prices, which constitute a large portion of the consumer shopping basket in these countries, have stabilised. Inflation in Georgia is in negative figures, with consumer prices falling by 2.2% year on year in March 2012. Belarus experienced very high inflation last year, following significant devaluation of the Belarusian ruble. However, the authorities have begun to contain inflation by a combination of tighter monetary policies and directed lending policies, as well as administrative food price control measures. As central banks in the region expect inflationary pressures to remain subdued in the near term, monetary policy in most of the countries has been loosened.

After increasing in late 2011, balance-of-payments pressures have subsided somewhat. Most of the countries were able to replenish their external reserves in the spring of 2012. Remittance inflows have increased in Armenia, Georgia and the Republic of Moldova. The stocks of non-performing loans have been decreasing from previous crisis peaks, although they remain elevated in several of the countries. The region's access to international capital markets remains limited.

The region's vulnerabilities remain significant due to its reliance on external demand to support growth, terms of trade pressures (as all countries except Azerbaijan are net energy importers, and the Caucasus countries depend on imports of foodstuffs) and the volatility of remittances. Risks to the outlook are related to developments in external demand, commodity prices, and stability of the domestic and, in some cases, broader European financial sectors, as well as domestic policy slippages, which may in some cases threaten needed international support.

Table 1.2. **Main macroeconomic indicators for Eastern Partner countries, 2011**

Indicator	Unit of measurement	ARM	AZE	BLR	GEO	MDA	UKR
GDP growth	Per cent, y-o-y	4.7	0.1	5.3	7	6.4	5
CPI inflation	Per cent, average	7.6	8.5	52.9	8.5	7.2	7.7
Government balance	Per cent of GDP	–2.7	13.3	3.3	–3.6	–2.4	–4
Current account balance	Per cent of GDP	–12.3	26.3	–10.4	–12.7	–10.6	–3.9
Net FDI	USD million	590	87	3 928	921	261	6 300
External debt	Per cent of GDP	65.5	7.7	61.1	53.1	67	76.2
Gross reserves	Per cent of GDP	18.2	16.7	12.4	20.3	30.3	22
Nominal GDP	USD billion	10.1	62.3	55.5	14.3	7	162.9

Source: EBRD (2011) data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks.

SMEs in the EaP countries: An important source for future growth and employment

SMEs in the EaP countries account for over 95% of private enterprises; they make a significant contribution to job creation and are behind the expansion and creation of added value in a number of sectors which drive economic growth and development (OECD, 2010). As in other transition countries, SMEs in the EaP region are an important source of jobs especially for low-skilled labour, young people and women (WBCSD, 2007) and are more likely to compensate for unemployment related to the down-sizing of the public sector (Woodward, 2001).

Promoting the SME sector in the EaP region is a cost-effective way for governments to support a shift from a centrally-planned to a market economy and making efficient use of assets that are privatised or liquidated (Smallbone, 2001). SMEs facilitate the adjustment of the economy from highly concentrated industries focused on mass production to a more flexible production process and demand-oriented supply of products. SMEs are more flexible and have the potential to provide a supply basis for larger enterprises by occupying niches that are free at various levels of supply chains. They are an important source of local knowledge, which is especially useful for international investors entering the markets or large corporations that do not have enough expertise in the region.

However, when comparing the performance of SMEs in EaP countries to that of OECD members, aggregate estimates indicate that despite employing almost 50% of a country's employed (*versus* 60-70% in OECD economies), their contribution to GDP is on average just over 30% (*versus* 55%).

The issue is that most SMEs in the EaP countries operate in lower-value-added sectors such as wholesale and retail trade in which companies mostly generate turnover instead of value added. Generally speaking, SMEs in the region are concentrated in sectors which tend to have lower entry barriers (*e.g.* less regulated sectors) and do not require high upfront investment or skilled labour to start business operations (*e.g.* not being in production). There are various reasons why business owners may choose to focus mostly on trade and the service sectors, including significant resource constraints and a lack of skilled labour, higher risk aversion of business owners and limited capabilities to compete effectively in productive industries.

As a result, most SMEs in the EaP region are microcompanies which consist of fewer employees and which operate mainly with the objective of generating personal income to

Box 1.2. **Defining SMEs**

SMEs are generally firms that are relatively small in size in terms of employment, turnover and total assets. Despite a common concept of what SMEs are, each country has its own definition for the SME sector. The way it is defined largely depends on the economic environment, the size of the country and the economic importance attached to a certain grouping of companies (OECD, 2011a). In the EU, in particular, the definition for SMEs is based on three criteria: employment, turnover and balance sheet total (see Table 1.3).

Table 1.3. **EU definition of SMEs**

Enterprise category	Headcount	Turnover	or	Balance sheet total
Medium-sized	< 250	≤ EUR 50 million		≤ EUR 43 million
Small	< 50	≤ EUR 10 million		≤ EUR 10 million
Micro	< 10	≤ EUR 2 million		≤ EUR 2 million

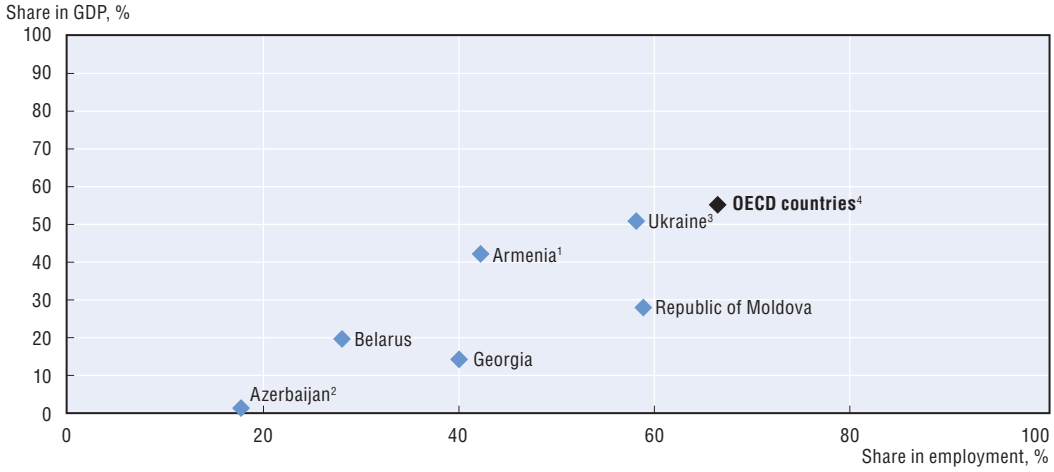
Source: European Commission (2003), Recommendation 2003/361/EC concerning the "Definition of Micro, Small and Medium-sized Enterprises", 6 May 2003.

In the Eastern Partner countries, definitions of the SME sector differ: Armenia, Belarus and the Republic of Moldova define micro, small, and medium-sized firms. Georgia and Ukraine define small and medium-sized enterprises. Azerbaijan defines small entrepreneurship as one single category for micro, small and medium-sized firms. In this report, the terms used for small business are SMEs, SME sector or small business, which in all cases includes the entire small business sector as defined by the national legislation of each country.

make a family living. In Armenia, Belarus and the Republic of Moldova, in which a category for microcompanies exists, more than 75% of companies employ less than 10 people (Belarus: less than 15). By default, the contribution to employment is relatively low, ranging between 8% and 15%. Similarly, the contribution to value added stays below 10% in this company segment.

This concentration of companies in lower-value-added sectors and a lack of interest by business owners in growing, investing and employing have important implications for policy makers. It shows that entrepreneurial activity in many cases is not motivated by the quest for business opportunities but rather is stimulated by mere necessity, forcing individuals to pursue self-employment and generate income. While stimulating self-employment has an important social value, "necessity entrepreneurship" does not drive business expansion and economic growth based on generating new ideas, transferring knowledge and taking risk. SMEs that produce economic value are rather those driven by opportunity and that have the ability to act on it by introducing new products and processes, tapping new markets and finding their niche in regional and global value chains. The EBRD Transition Report even argues that policy makers may wish to focus solely on promoting "opportunity entrepreneurship" if policies are at odds with those encouraging business starters (EBRD, 2011).

Figure 1.1. **SME sector contribution to employment and GDP in EaP countries, 2010**



1. The data from Armenia is based on registered enterprises (as opposed to active enterprises).
2. The contribution of SMEs to GDP in Azerbaijan does not include individual entrepreneurs.
3. In Ukraine turnover data is used instead of GDP, as data on share of SMEs in GDP is not available.
4. The OECD average is based on the simple average among 30 OECD countries from OECD (2011), *Entrepreneurship at a Glance* 2011.

Source: SME DNC (2010) (Armenia), based on Ministry of Justice Legal Entities State Registry Agency; State Statistical Committee of the Republic of Azerbaijan (Azerbaijan); Department of Entrepreneurship of Ministry of Economy of Belarus and National Statistical Committee Belstat (Belarus); Entrepreneurship in Georgia (2010) and GeoStat, Business Statistics, as of 1 March 2012 (Georgia); National Bureau of Statistics of the Republic of Moldova (Republic of Moldova); State Committee of Ukraine for Statistics (Ukraine); OECD (2011), *Entrepreneurship at a Glance 2011*, OECD, Paris.

Policy barriers limit SMEs' growth perspectives in the EaP region

A number of surveys carried out across the EaP region indeed confirm that most entrepreneurs are focussing on keeping their company alive without the intention of growing their business, rather than on expanding into new markets or engaging in innovative activities. The reasons given are, to a large extent, persisting policy barriers which limit SMEs' growth perspectives.

According to the joint EBRD/World Bank Business Environment Enterprise Survey (BEEPS) 2008-09,[4] in EaP countries the greatest common obstacles to growth identified by firms participating in the survey are: limited access to finance, unfavourable tax rates and political instability. These obstacles coincide with those identified by firms in the Eastern Europe and Central Asia region as a whole. Even though these obstacles are pointed out by firms of all sizes, the share of small and medium-sized firms affected is typically larger.

Access to finance is referred to as the number one obstacle in Azerbaijan, Georgia and the Republic of Moldova. It also disproportionately affects small firms in Azerbaijan and Georgia, where more than 20% of small firms identified it as an obstacle to growth. (More detailed information on the BEEPS access to finance results is provided in Chapter 8 of this report.) Tax rates are seen as a major obstacle in Belarus, where 72% of small firms and 52% of medium-sized firms identified tax rates as a major constraint. Tax rates were the second major obstacle in Armenia, Azerbaijan and Ukraine. Political instability was found to be a major obstacle for firms of all sizes in Ukraine, but also in Armenia and Georgia.

Apart from these barriers which limit SME growth in most countries of the region, there are some specific policy areas which were indicated by SMEs in some countries as barriers for growth. According to the BEEPS 2008-09, 18.2% of surveyed firms in Azerbaijan,

10.6% in Ukraine and 10.1% in the Republic of Moldova have identified corruption as a major constraint for doing business. In Armenia, the practices of the informal economy are a major issue for both SMEs and large firms. In Belarus, business licensing is seen as one of the key obstacles, particularly for small firms (52%). Also, in Belarus and the Republic of Moldova, an inadequately educated workforce was identified as one of the major obstacles by a large share of surveyed firms (14.1% and 15.7% respectively).

Box 1.3. **Policy barriers for SMEs with export orientation**

To complement the policy perspective given in this report with the views of the private sector in the EaP region, a report has been prepared by EUROCHAMBRES in the framework of the East Invest programme. East Invest is an initiative of the European Union which promotes investment and economic co-operation between the EU and EaP business communities. There is a strong focus on strengthening business representative organisations in the six EaP countries, and providing direct support to SMEs to develop business with the EU.[1]

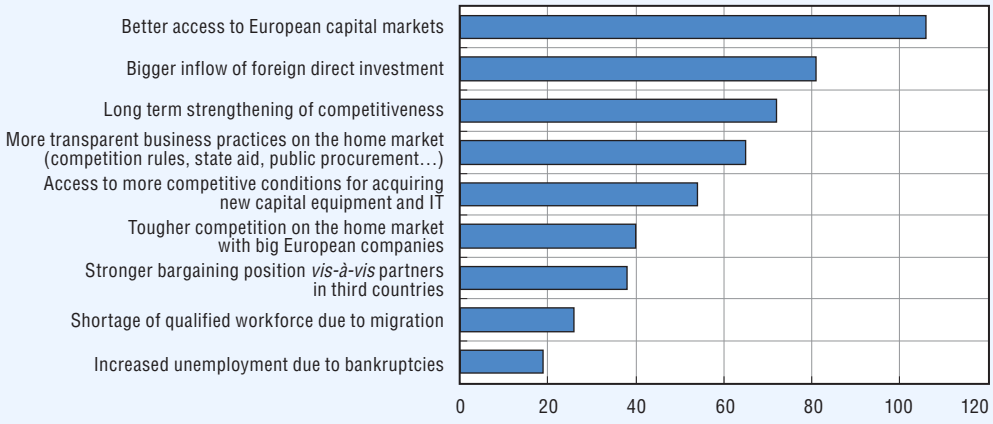
EUROCHAMBRES aims at facilitating communication and exchange of experiences, information and best practices within the network of Chambers of Commerce while offering services and tools for the Association and its members from 45 European countries. Activities range from external communications to the management of international exchange programmes between Chamber experts, and from training to the implementation of new technologies.

A survey was conducted among 200 SMEs from the six EaP countries that have participated in a training programme around internationalisation and the EU *acquis*. The sample is not representative as it is based only on SMEs that have an international orientation. SMEs were asked to share their perceptions on EU integration, key factors of competitiveness, barriers to investment, and other key areas affecting their businesses. Below are some of the results; a more detailed report is available at EUROCHAMBRES.[2]

EU integration should mainly bring positive elements

Asked about the possible impact on their activities of closer integration with the EU (mainly through DCFTA negotiations), most SMEs are optimistic: they expect better access to European capital markets and hope for increased FDI into their country. SMEs seem less concerned with the "threats" of increased competition, as shown in the figure below.

Figure 1.2. **How do SMEs see the impact of DCFTA negotiations**



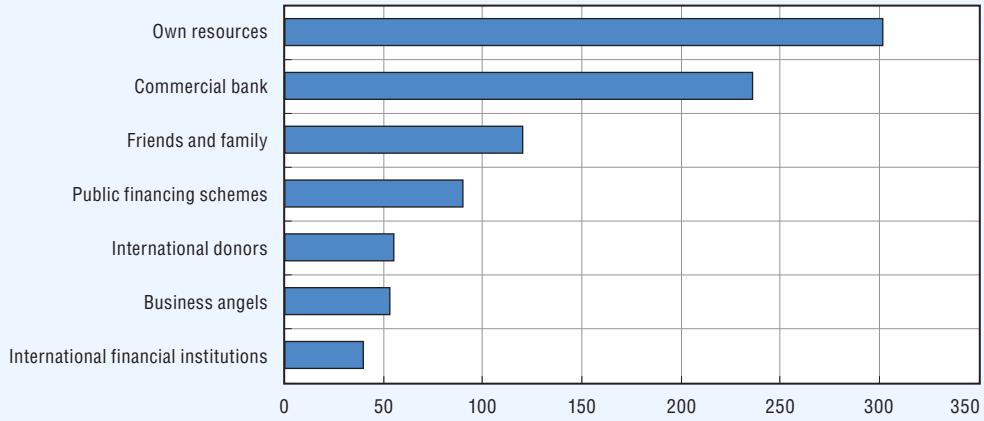
Note: The points given by the companies are based on a survey question where companies could allocate 1 point to each item they considered to be relevant (allowing multiple choice). The maximum number of points that could be allocated per item is 200.

Box 1.3. **Policy barriers for SMEs with export orientation** *(cont.)*

Access to finance underdeveloped

Focusing on their sources of finance, SMEs in EaP countries confirmed that business is primarily financed through their own funding. Local banks are used regularly, but access to international funding schemes seems to be underdeveloped.

Figure 1.3. **What are SMEs' primary financing sources**



Note: The points given by the companies are based on a survey question where companies were asked to rate the sources of finance from 1 to 3, with 1 = least important, 3 = most important. The maximum number of points per item is 600.

Source: East Invest Survey 2012, forthcoming report to be published by EUROCHAMBRES in the framework of the East Invest project.

1. For more details on East Invest: *www.east-invest.eu*.
2. Contact at EUROCHAMBRES: Ms. Birgit Arens, *arens@eurochambres.eu*.

SME policy: A tool to foster SME performance in the EaP region

To address these challenges, EaP countries would benefit from looking at comprehensive responses to SME competitiveness challenges. Promoting SMEs is necessary as they do not have significant business power, starting with bargaining power on government policies and access to finance and ending with increased administrative and production costs. Small enterprises do not have the ability to influence nation-wide policies and/or use economies of scale to reduce costs. Moreover, many large firms in the EaP countries today were initially created on the principle of size and not efficiency.

Comprehensive SME policy frameworks are based on a mix of sound horizontal policies creating a favourable business environment for the entire enterprise population and targeted interventions to address specific information, market and co-ordination failures with an impact on SMEs. The first objective can, to a certain extent, already be achieved by reducing administrative barriers for business activities, whereas the second objective requires implementing specific support measures that help SMEs overcome negative externalities. There is a need for effective policy co-ordination across the ministries involved in the process to ensure that policy making addresses both objectives in a comprehensive manner.

In the EU, considerable progress has been made over the past few years in creating a business environment conducive to the development of SMEs. The European Commission has made progress in cutting red tape for SMEs and the focus on SMEs in major EU support

programmes has been significantly increased. A major political initiative to fully exploit the potential of European SMEs was the adoption of the Small Business Act (SBA) for Europe by the European Commission in 2008. The SBA focuses on a general climate in society that should lead individuals to consider the option of starting their own business as an attractive venture. Therefore the perception of the role of entrepreneurs and risk taking in the EU would have to change: entrepreneurship and the associated willingness to take risks should be strongly supported by administrations. Being SME-friendly should become mainstream policy, based on the "think small first" principle.

All EaP countries have started to develop instruments to support SMEs and entrepreneurship. However, this is largely done on an *ad hoc* basis. In countries which have begun to institutionalise mechanisms for SME policy making, such as Armenia and the Republic of Moldova, the policy has strong elements of a social policy which yields results with regards to an increased share of employment stemming from SMEs (between 42% and 58%). Both countries implement a number of programmes specifically targeted towards the unemployed, providing start-up support and entrepreneurship training.

However, as argued before, SME policy should also be seen as an economic growth policy and EaP countries are well advised to develop appropriate policies that target companies with a high-growth perspective. In a market economy, successful large firms grow out of the SME sector and need to inherit key principles that drive economic growth such as efficiency and innovation. In OECD economies, high-growth SMEs largely contribute to the innovation process and are often active in breakthrough innovations (OECD, 2010). It is therefore important to promote SME growth to shift from subsistence SMEs to a culture of entrepreneurship which gives SMEs the possibility to prosper and to contribute to the country's economic growth and development.

Conclusion

The OECD research that has been developed over the past decades reinforces these findings by emphasising the importance of promoting and developing the private sector by improving the environment for SMEs and entrepreneurship. This translates into policies which seek to create a level playing field for SMEs through regulatory reform, the removal of administrative burdens, and mechanisms that strengthen the conditions for the diffusion of technology and the upgrading of skills. Policies should be consistent with a horizontal approach to policy making, seeking to improve conditions for the largest possible number of enterprises. They should be designed to tackle development concerns such as job creation, economic growth, poverty reduction and social inclusion.

Notes

1. Regional average of GDP growth, weighted with country GDP, based on data from EBRD (2011), *Crisis in Transition: The People's Perspective*, Transition Report 2011, EBRD, London.
2. Data for Azerbaijan, the Republic of Moldova and Ukraine is from 2009, data for Armenia and Georgia is from 2008; data for Belarus is not available. According to the Statistical Committee of the Republic of Azerbaijan, unemployment in 2011 represented 5.4%.
3. European Union, *European Union External Action*, *www.eeas.europa.eu/eastern/index_en.htm*; ENPI Info Centre, *www.enpi-info.eu/eastportal/news/latest/22206/EU-launches-negotiations-on-Association-Agreements-with-Armenia,-Azerbaijan-and-Georgia*.
4. Business Environment Enterprise Survey (BEEPS) is a comprehensive company-level data survey in emerging markets and developing economies conducted as a joint initiative of the European Bank

for Reconstruction and Development and the World Bank Group. Due to its detailed questionnaires, the data can be broken up by size of firms, allowing a detailed analysis of the obstacles that small and medium-sized firms face compared to large firms, where small and medium-sized firms are defined as firms of 5-19 and 20-99 employees respectively. For the EaP countries the latest survey was conducted in 2008 and 2009. The results are based on interviews conducted with 1 035 firms in the manufacturing sector.

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PART I

Chapter 2

Approach and overview of the Small Business Act assessment process

The SME Policy Index *measures progress in the implementation of SME policy reforms based on the principles of the EU Small Business Act (SBA). It aims to support SME policy development in the six Eastern Partner (EaP) countries and give guidance for policy reform. The SBA assessment process was introduced to EaP countries in May 2010 as a tool to support governments in developing a comprehensive policy framework conducive to SME growth. The assessment builds on the experience of the Western Balkans and the Euro-Med region in which similar policy assessments have successfully been carried out.*

Introduction

The *SME Policy Index 2012* aims to support SME policy development in the six Eastern Partner (EaP) countries participating in the OECD Eastern Europe and South Caucasus (EESC) Initiative (Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine). The OECD together with the European Commission, the European Training Foundation (ETF) and European Bank for Reconstruction and Development (EBRD), has developed a framework for co-operation under the umbrella of the Eastern Partnership Platform 2 on Economic Integration and Convergence with EU policies.

The EU Small Business Act (SBA) provides a comprehensive SME policy framework, promotes entrepreneurship, and anchors the "think small first" principle in law and policy making to strengthen SME competitiveness. Built around ten principles and several concrete policy and legislative actions to implement them, the SBA invites both the European Commission and EU member states to tackle the obstacles that hamper SMEs' potential to grow and create jobs (European Commission, 2011).

The political context of the Eastern Partnership

The Eastern Partnership (EaP) was launched in May 2009 at a summit in Prague as an initiative to help promote political and economic reforms, and enhance the EU's political and economic co-operation with six countries from the Eastern Neighbourhood region (Armenia, Azerbaijan, Belarus, Georgia, the Republic of Moldova and Ukraine) within a long term perspective. The EaP is a political project aiming at projecting stability and prosperity to Eastern Europe and the South Caucasus with large strategic interests for the EU (energy security).

This engagement combines a call for deeper bilateral relations, including new Association Agreements with Deep and Comprehensive Free Trade Agreements (DCFTA) coupled with an innovative strategy to enhance co-operation between neighbours. Negotiations for DCFTAs have been offered to all six EaP countries as the main instrument for developing closer ties with these countries and bring more economic stability and predictability in the region. Negotiations for a DCFTA have been finalised with Ukraine, and were launched with the Republic of Moldova, Georgia and Armenia.

The second Eastern Partnership Summit held in Warsaw in September 2011 reaffirmed the agenda agreed in Prague and acknowledged that important progress had been made in a number of areas. However, the Summit participants also recognised that the reform efforts needed to be reinforced.The multilateral co-operation is co-ordinated through four thematic platforms:

- democracy, good governance and stability (platform 1);
- economic integration and convergence with EU policies (platform 2);
- energy security (platform 3); and,
- contacts between people (platform 4).

The platforms and the panels organised under each platform, bring together EaP and EU government official at senior or expert level, with the purpose to familiarise EaP officials with EU policies and identify directions for co-operation.

The European Commission (DG Enterprise and Industry) plays a prominent role in the management of the economic dialogue with the EaP countries by chairing the platform on "Economic Integration and Convergence with EU Policies" which meets twice a year. A series of co-operation areas are covered by the platform ranging from trade and trade related regulatory co-operation, macroeconomic and financial co-operation, socio-economic development, environment and climate change to transport. In its first meetings, the platform identified a limited number of priorities where co-operation should be intensified and established four panels (subgroups of the platform) on "Trade and Trade Related Regulatory Co-operation linked to DCFTAs", "Environment and Climate Change", "Transport" and "SME Policy".

Within the scope of the platform 2 on "Economic Integration and Convergence with EU Policies", a specific SME Panel has been established in 2010 which is also chaired by DG Enterprise and Industry. Its purpose is to exchange information on SME policy approaches in the EU and in the Eastern Partner Countries. The Panel is supported by a multilateral project involving the OECD, the European Training Foundation and EBRD which is developing the *SME Policy Index* for the Eastern Partner countries. In addition, the Panel covers the implementation of the "SME Flagship Initiative" of the Eastern Partnership.

The Small Business Act assessment process in the Eastern Partner countries

The Small Business Act (SBA) assessment process was introduced to EaP countries in May 2010 as a tool to support governments in developing a comprehensive policy framework conducive to SME growth (European Commission, 2011). The assessment builds on the experience of the Western Balkans and the Euro-Med region in which similar policy assessments measuring the approximation to the European Charter for Small Enterprises and, since 2008, the EU Small Business Act were carried out by the OECD in 2006, 2009 and 2012 in collaboration with its partner organisations.

Based on this experience and to ensure both national and regional ownership of the assessment process, every EaP country nominated a national SBA co-ordinator who participated in all stages of the process, *i.e.* design of policy indicators, co-ordination of data collection, application of the assessment tool through a government self-evaluation, and discussion of results at both national and regional levels.

The assessment process was carried out between October 2010 and October 2012 in three phases:

- *Design phase (October 2010-March 2011):* EaP countries participated in an OECD Working Group meeting which took place back-to-back with an EU SME Panel meeting in October 2010 and two regional workshops in March 2011 to define the scope of the assessment and agree on the structure of the indicators.
- *Evaluation phase (April 2011-January 2012):* EaP countries carried out a self-evaluation of their policy frameworks in two assessment rounds which was complemented with independent assessments carried out by the OECD, the European Commission, the ETF and EBRD with the support of local consultants. A discussion on initial findings, during which EaP countries made a commitment to develop targeted policies supporting SMEs and entrepreneurship (Annex B), took place at the regional level in June 2011. In addition, an OECD policy seminar on SME policy tools based on the Small Business Act was held in October 2011.

Box 2.1. **Key steps in the SBA assessment process 2010-12**

May 2010 – Presentation of the Small Business Act as an Assessment process to EaP countries in a meeting of the Eastern Partnership Platform 2 on "Economic integration and convergence with EU policies".

October 2010 – Agreement between partner organisations (European Commission, OECD, EBRD and ETF) and EaP countries to carry out a policy assessment based on the principles of the EU Small Business Act.

October 2010 – First meeting of the EU SME Panel and OECD Eastern Partnership Enterprise Policy Development Working Group.

March 2011 – Two workshops held in Brussels and Torino to finalise and endorse a set of policy indicators with SBA co-ordinators to measure SME policy performance in the EaP region based on the EU Small Business Act.

April-June 2011 – Self-evaluation by EaP countries on a first set of principles.

June 2011 – Second meeting of the EU SME Panel and OECD Eastern Partnership Enterprise Policy Development Working Group, back-to-back with the OECD Ministerial Conference in which EaP countries adopted a Ministerial Declaration on "Fostering SMEs, Entrepreneurship and Competitiveness" agreeing to develop targeted policies to support SMEs and entrepreneurship based on the guiding principles of the EU Small Business Act.

June-October 2011 – Independent assessment carried out by OECD, European Commission, EBRD and ETF with the support of local consultants.

October 2011 – Capacity building seminar held in Trento, Italy, in collaboration with OECD LEED Trento Centre.

November 2011-January 2012 – Self-evaluation by EaP countries on a second set of principles.

February-March 2012 – Bilateral stakeholder meetings in all six EaP countries to consolidate findings of self-evaluation and independent assessments.

April 2012 – Regional workshop held in Kyiv, Ukraine to consolidate findings at the regional level and discuss aggregated scores.

May-July 2012 – Report is finalised and published.

October 2012 – Launch of *First SME Policy Index: Eastern Partner Countries 2012*.

- *Consolidation phase (February 2012-October 2012):* Bilateral stakeholder meetings were held in all six EaP countries to consolidate findings from self-evaluations and independent assessments. The final report was prepared following a discussion at the regional level which took place in April 2012 in Kyiv, Ukraine.

To complement the assessment process with a component on regional policy dialogue and the exchange of best practices on enterprise policy, the OECD established an Eastern Partnership Enterprise Policy Development Working Group, co-chaired by the European Commission (DG Enterprise). Meetings of the Working Group were held back-to-back with meetings of the EU SME Panel in October 2010 and June 2011. The Working Group involves both SME policy makers and business community representatives from EaP countries:

- The first working group meeting was held on 25 October 2010 in Brussels. The OECD and its partner organisations presented the proposed project to representatives from all EaP countries. The Republic of Moldova presented a case study on the project methodology which had already been applied in the country as part of bilateral co-operation with the OECD. All six partner countries agreed to pursue a similar approach for the EaP region based on a common policy assessment framework derived from the EU Small Business Act.

- The second working group meeting was held on 15 June 2011 in Prague, the Czech Republic, back-to-back with an OECD Ministerial Conference on Competitiveness and Enterprise Policies for Eastern Europe and the South Caucasus (17 June). The working group meeting provided a forum for the exchange of best practices and a discussion of initial findings of the enterprise policy performance self-evaluation. Experts from Poland and the Czech Republic presented case studies of how to develop a comprehensive SME policy and how to establish an effective mechanism for public-private dialogue. As part of the meeting, a business roundtable was organised as a platform for dialogue between potential investors and the EaP delegations. All partner countries presented business opportunities and met CEOs from about 50 companies, on a bilateral basis. The roundtable was hosted by the Confederation of Industry of the Czech Republic in co-operation with the OECD Business and Industry Advisory Committee (BIAC).
- A third meeting is envisaged to take place in October 2012 during which this report will be launched.

In addition to the working group, on 24-28 October 2011 the OECD held a capacity-building seminar for SBA co-ordinators and experts from the EaP region in Trento, Italy in collaboration with the OECD LEED Trento Centre. It focussed on SME policy tools with a selection of themes identified as priorities during the assessment process (business co-operation and local governance; technology, innovation and green growth; access to finance). The seminar gave participants from the region the opportunity to present and discuss case studies and exchange best practices on SME policy development. It provided participants with a more practical understanding of the instruments promoted by the EU Small Business Act.

Importance and relevance of the Small Business Act

The evaluation process in every partner country was co-ordinated by the relevant government institution in charge of SME policy or entrepreneurship development. Inputs were provided by relevant public administrations as well as independent consultants.

The added value provided by this evaluation framework is its holistic approach which provides policy makers with a single window to assess their progress in a specific context. The evaluation framework aims to:

- Independently and rigorously assess SME-related policy settings and reforms against international best practice.
- Give guidance for policy reform and development.
- Create a process that enhances the quality of policy development relating to SMEs.
- Facilitate the prioritisation of donor activities supporting SME growth.

While there are a number of other indices that assess the business environment in the countries of the EaP region, the evaluation framework of the *SME Policy Index* brings a different approach for addressing the SME policy issues. Main differentiating factors of the *SME Policy Index* from other indices from international organisations are:

- Focus on a very specific region where history, culture and geography allow for more relevant benchmarking between countries.
- Tripartite participatory approach to evaluation and measurement including government, private sector, and the OECD, European Commission, ETF and EBRD.
- Comprehensive evaluation of the SME policy environment structured along ten key principles in line with the EU Small Business Act.

- The index not only measures but also provides guidance on how to improve through good practices and policy recommendations.
- "Meta – Index" which incorporates existing work already conducted by other organisations (*e.g.* World Bank's *Doing Business* report).

The methodology has both strengths and limitations, presented in the Table 2.1 below.

Table 2.1. **Strengths and limitations of the *SME Policy Index***

Strengths	Limitations
• The indicators have been structured to be fully compatible with the EU Small Business Act. • Combination of original data collected by OECD, European Commission, ETF and EBRD with existing data from sources such as the World Bank or the United Nations. • Use of a common "scoreboard" facilitates public-private consultation and encourages action. • The "scoreboard" approach also helps public officials to communicate better with respect to policy progress and areas where more reform is necessary. • The *SME Policy Index* incorporates good practice examples and policy recommendations.	• Measuring effective implementation of government policy can be difficult. • Distinction between scoring levels can be challenged, especially when above 3. • A simple weighting system has been incorporated to give more important indicators a higher weight. • Not all dimensions have the same importance – the balance of this importance varies between countries. • There is a lack of general national statistics on SMEs, due to problems such as a uniform definition of an SME. • The *SME Policy Index* does not cover all aspects of SME policy but instead focuses on the areas covered by the EU Small Business Act. • 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.

Conclusion

EaP countries are invited to actively apply the *SME Policy Index* methodology as a tool to monitor progress in the implementation of SME policy reform on an ongoing basis. It gives direction to and helps build momentum in government policy towards the small enterprise sector across the EaP region. The SBA monitoring process (based on a participatory approach with the active contribution of government institutions, private sector representatives, non-governmental organisations and other SME stakeholders) is well positioned to enhance public-private policy dialogue at national level.

Reference

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PART II

Small Business Act assessment

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PART II

Chapter 3

Entrepreneurial learning and women's entrepreneurship (Dimension 1)

Create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded (Small Business Act Principle 1)

Promoting entrepreneurship across all levels of the learning system is an important driver for the economy and a critical building block for a more flexible workforce. Nevertheless, partnership building is required to ensure coherence in the sequence of entrepreneurship promotion across the learning system. Entrepreneurship as a key competence also requires particular attention in terms of curriculum and teacher training. The lifelong entrepreneurial learning agenda is relatively new and the identification and exchange of good practice should be encouraged. This will require more developed networks involving education and training providers both within the national education system and among those providing more general services. A support system for good-practice sharing in all countries is recommended. The assessment also focused on women's entrepreneurship where policy support is evolving. More developed advocacy networks will be important to ensure that women's entrepreneurship is factored into the competitiveness drive in each country.

Introduction

With increasing concerns as to the socio-economic effects of the global economic turn down, governments, the business world and social partners are confronted with two challenges: *a)* how to contain the crisis particularly in terms of its impact on employment; and *b)* to determine solutions for both jobs and growth for the longer term. These dual concerns have generated renewed interest in the contribution of education and training in the wider bid for economic recovery, employment and growth at national, regional and international levels. Particularly central to the dialogue is the potential of education and training in contributing to a more entrepreneurial culture. To this end, the European Union (EU) has drawn up policy recommendations for entrepreneurship promotion across all levels of education. These have been reinforced through the EU's 2020 "jobs and growth" strategy (EU, 2009) and the Small Business Act (SBA) with specific emphasis on promoting "entrepreneurial mindsets amongst young people" (European Commission, 2008, p. 6). At global level, a similar policy thrust has been put forward by the World Economic Forum (2009).

While the policy response within the EU to the Small Business Act in terms of defining strategies to bring forward the recommendations for entrepreneurship promotion has been mixed (Eurydice, 2012), EU aspirant countries have embraced the agenda, building on a momentum of strategic reviews of entrepreneurship in education and training initiated under the European Charter for Small Enterprise (Gribben, 2012). This policy drive has been brought forward under the Small Business Act and where all countries in the EU pre-accession region have committed to regular reviews set against a set of pre-defined indicators for each level of the learning system.[1]

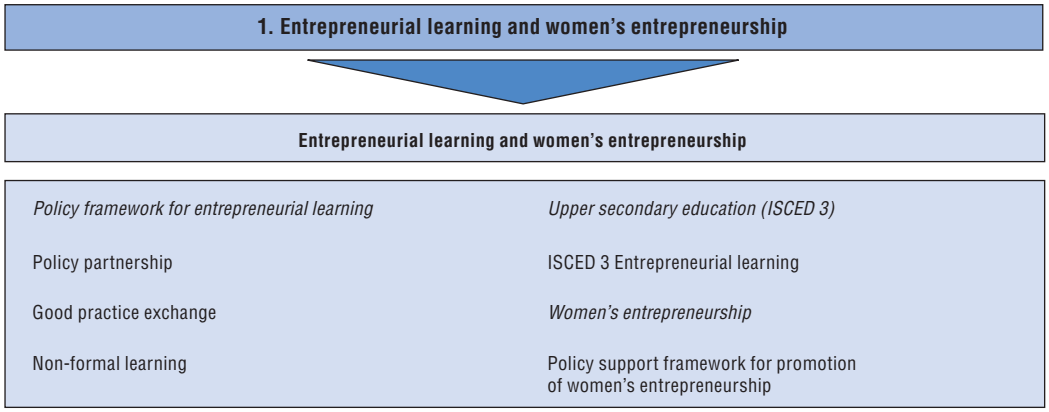
In addition, the global economic crisis has generated new interest in how women can be better integrated into the economy (UN, 2011) with the EU's Small Business Act, with specific attention to women's entrepreneurship. The crux of the issue is that women's entrepreneurship can no longer be defined simply in terms of social inclusion. Rather, the disruption to the global economy is prompting a more strategic rethink of women's entrepreneurship in terms of competitive business. To this end, the European Union has taken steps to generate greater understanding of the contribution of women's entrepreneurship to the competitiveness agenda including the promotion of mentoring schemes to support women's start-ups and growing businesses (European Commission, 2011).

This chapter considers the issues and outcomes of the assessment of the EU's Eastern Partner (EaP) countries in promoting entrepreneurship through education and training. It also considers women's entrepreneurship. The chapter closes with recommendations to bring forward developments in both areas.

Assessment framework

For the purposes of this assessment, five indicators were adopted by the EaP countries as part of the wider set of indicators addressing the range of policy areas covered by the SBA. The indicators were borrowed from an existing policy assessment package already used by the countries of the EU's pre-accession region in their efforts to meet the SBA policy recommendations.[2]

Figure 3.1. **Assessment framework for Dimension 1: Entrepreneurial learning and women's entrepreneurship**



Entrepreneurial learning and women's entrepreneurship dimension covers three sub-areas. The first area considers the policy support framework for entrepreneurial learning, particularly in terms of how the partners involved across the learning system co-operate to ensure a comprehensive policy support framework. The second area looks at entrepreneurship key competence development in upper secondary education, particularly entrepreneurial learning at ISCED 3 level. The third area assesses how governments support promotion of women's entrepreneurship. Before introducing the five indicators, clarification on the terminology used within the wider assessment of the first dimension of the SBA is important.

The dimension refers specifically to entrepreneurial learning as opposed to entrepreneurship education. This is because EU education policy which addresses entrepreneurship promotion goes beyond the narrowly-defined notion of entrepreneurship and business start-ups to include the wider value of entrepreneurship promotion for the individual within the schooling system in terms of employability, creativity and innovation. Put simply, while "entrepreneurship" conveys a sense of business or commerce, "entrepreneurial", as a complimentary concept, captures more fully a sense of the mindset, spirit and behaviour of an individual. It is this factor which lies behind the EU concept of entrepreneurship as a "key competence" (EU, 2006) – a set of cognitive and behavioural traits which make up the entrepreneurial individual who is able to bring initiative and added value to the workplace.

Secondly, while "education" reflects more what happens inside the formal schooling and university system, "learning" is a broader, more inclusive concept. It recognises the value of family, culture, personal experience and know-how acquired outside the school (informal learning). Learning also includes education and training not subject to formal

assessment or examinations (non-formal learning), for example through on-the job training. Both informal and non-formal learning are considered critical to the development of an entrepreneurial culture.

For the purposes of the assessment, therefore, entrepreneurial learning is defined as "all forms of education and training, formal, informal and non-formal, which contribute to an entrepreneurial spirit and behaviour with or without a commercial objective".[3] The crux of the issue is that entrepreneurial learning not only prepares people for business careers but, as importantly, ensures that employees behave more entrepreneurially on the job, creating a more productive business environment (Bosma, Wennekers and Amoros, 2012).

Policy partnership

The rationale behind the policy partnership indicator is that a sequenced development of entrepreneurial learning across the education system, including how this interfaces with what happens outside formal schooling, will contribute to more efficiency and effectiveness of the overall entrepreneurial learning effort. More specifically, the objective of the indicator is that all stakeholders (government, private sector and civic interest groups) co-work the entrepreneurial learning agenda as a collective or partnership. An important feature of the indicator is that the partnership arrangement ensures coherence between developments in entrepreneurial learning and wider policies in the country (*e.g.* education, SME, employment, innovation) creating a mutually-reinforcing entrepreneurship eco-system.

Good practice exchange

This indicator encourages those involved in lifelong entrepreneurial learning to share their experience regularly and systematically allowing for greater efficiency in the design and delivery of entrepreneurial learning. An important feature of the indicator is the structured build-up of intelligence and access to good practice in entrepreneurial learning. A final feature of the indicator is international co-operation: the opportunity and benefits of sharing good practice domestically, between the EaP countries, and beyond.

Non-formal learning

The rationale behind the indicator on non-formal entrepreneurial learning is that many organisations outside the schooling system (*e.g.* chambers of commerce, regional development agencies, private training providers) make a considerable contribution to knowledge, skills and know-how for business start-ups, in particular. Community-based organisations and NGOs also very often play a role in nurturing the entrepreneurship key competence and primary business skills of specific target groups (*e.g.* youth, women, immigrants). The value-added of non-formal entrepreneurial learning is in the customised approach to its design and delivery, including flexibility in terms of timing and location. The indicator additionally encourages providers of non-formal learning to showcase and to promote know-how transfer of successful projects.

Given a significant effort in all countries in developing continued vocational training, there is clearly an opportunity to determine how entrepreneurship promotion could be reinforced in this area.

Entrepreneurial learning in upper secondary education

The fourth indicator in the assessment considers how the entrepreneurship key competence and first business skills are addressed in upper secondary education (ISCED 3). With the specific objective of scale and sustainability, the indicator particularly focuses on the extent to which the entrepreneurship key competence and more developed entrepreneurship skills are embedded in the national curriculum. The upper reaches of the indicator examine how the curriculum is addressed within the schooling system. While this assessment focuses particularly on upper secondary education, links with earlier education and higher education are important, particularly in terms of ensuring the sequence of entrepreneurial learning across the system. Hence, upper secondary education should build on entrepreneurial learning developments in primary and secondary education. Continuity in key competence promotion is particularly important here.

Policy support framework for promotion of women's entrepreneurship

The final area assessed looks at the national policy framework for women's entrepreneurship. Given the range of policy areas which directly affect women's entrepreneurship potential (social, economic, employment, fiscal, education), the indicator firstly encourages the EaP countries to ensure dialogue, understanding and coherence between the policy areas. This requires a dedicated policy partnership, including a strong advocacy framework backed up with an implementation plan which includes monitoring of the respective policy areas; financial support for delivery of the plan is also important.

Analysis

This section considers the findings from the region. More developed detail on the results per country is addressed in the country-specific chapters. The results of the assessment for entrepreneurial learning and women's entrepreneurship are provided in Table 3.1. Two performance clusters are clearly identifiable: Armenia, Azerbaijan and Georgia are above the regional average weighted scoring of 2.23 with the remaining countries following closely.

Table 3.1. **Scores for Dimension 1: Entrepreneurial learning and women's entrepreneurship**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
1.1.1.	Policy partnership	2	2	1	4	2	2
1.1.2.	Good practice exchange	1	1	1	3	1	1
1.1.3.	Non-formal learning	1.5	2	1.5	1.5	1	1
1.1.4.	ISCED 3 Entrepreneurial learning	4	4	3	3	2	2
1.1.5.	Policy support framework for women's entrepreneurship	2.5	2.5	1.5	3	3	1.5
Weighted score		***2.40***	***2.45***	***1.60***	***3.15***	***2.10***	***1.65***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Overall, Georgia stands out for its promising performance on this SBA dimension.

In terms of women's entrepreneurship, Azerbaijan, Georgia, and the Republic of Moldova demonstrate more developed partnership approaches to policy development while the efforts of Belarus and Ukraine in reviewing policies for gender sensitivity are an important step.

Policy framework for entrepreneurial learning is developing across the region

As regards entrepreneurial learning, while policy partnership overall will require more considered attention, the assessment points to good efforts in most countries in entrepreneurship promotion in upper secondary education. However, the assessment underlines the need for more concerted efforts in the sharing of good practice and where networking and exchange between the non-formal entrepreneurial learning providers will be important.

Policy partnership

The most important finding from the assessment on policy partnership for entrepreneurial learning is that most countries are already engaged in cross-stakeholder discussions although the degree of co-operation and composition of the institutions involved varies from country to country. While the dialogue process tends to be linked to wider systemic-based developments in the education and training process (*e.g.* as part of the qualifications' framework discussions in Ukraine or addressed within a social partnership drive for vocational education in Armenia), there is a need for a more concerted focus on entrepreneurial learning given the relative newness and challenges of that policy area. The Republic of Moldova already demonstrates initial steps here where the SBA assessment process has immediately engaged the education, training and employment authorities in the development of a national SME support strategy and where the SBA human capital concerns are an integral feature.

A next step for all countries will be to reinforce the dialogue process with a structured partnership arrangement to ensure continuity, development and monitoring and evaluation of policy. The partnership process should give equal attention to all parts of the formal education system, including the non-formal provider constituency, to create the conditions for a lifelong entrepreneurial eco-system. Leadership will be crucial to the success and sustainability of all partnership arrangements. While Belarus has still to establish a multi-stakeholder dialogue process for entrepreneurial learning, it already demonstrates a fundamental ingredient for any collective policy process: a presidential directive on entrepreneurship development. Where possible, consideration should also be given to building on existing networks or institutions which already have a good understanding of the entrepreneurial learning agenda. For example, in the case of Georgia, while the National Vocational and Training Council has a specific mandate for vocational learning, its policy framework could be extended to include a provision to address lifelong entrepreneurial learning.

Box 3.1. **The School Academy of Entrepreneurship in Ukraine**

The School Academy of Entrepreneurship project was launched in Ukraine following the "Leaders of Education" initiative – a grass-roots drive to generate understanding, capacity and commitment to entrepreneurial learning. It involves a network of 100 pilot schools across ten regions. Supported by the Polish government, the academy gives specific attention to entrepreneurship as a key competence. Teachers are the primary focus for change and innovation. Students establish entrepreneurship clubs within pilot schools. The schools work in clusters with spin-off for networking and good practice exchange, using the e-learning approach. Finally, the developments around the schools are fed back up to the national level with the objective of generating scale and sustainability for the entrepreneurial learning effort across the school network.

Good practice exchange

Overall performance on good practice in the promotion of entrepreneurial learning across the region was weak. This is principally due to a lack of structured networks for exchanging experience and know-how specifically on entrepreneurial learning. Nonetheless, the Adult Education Association of Georgia provides an excellent example of how post-secondary education outlets network and share developments on entrepreneurship promotion, as well as with secondary and tertiary vocational education. Connecting down to earlier entrepreneur promoters in early education would be a logical next step.

Aside from networks, the assessment pointed to examples of where good practice in entrepreneurial learning is being accommodated in the national education and training environment. For example, the Baku Business Training Centre in Azerbaijan provides start-up training based on know-how from Germany supported by the GIZ, the German aid body. Additionally, the national employment service offers start-up training based on the ILO's KAB ("know about business") programme.

Given that entrepreneurial learning is an evolving policy area, it will take time for networks to form and become more active in sharing their experience. Support for development and reinforcement of networking should be considered by the national authorities and ideally involve a networking and good practice intelligence support system to allow for greater access to know-how. This will be important as the education and training provider market develops a greater interest in the area. A good example of a networking and good practice support framework from the EU pre-accession region is the Macedonian Centre for Entrepreneurship and Innovation which is behind a national network of entrepreneurship educators (formal and non-formal learning). The centre holds an annual convention to address new issues on the entrepreneurial learning agenda and where good practice is showcased.

Non-formal learning

The assessment points to an array of education and training providers promoting non-formal entrepreneurial learning. The Ministry of Finance in Georgia, for example, plays an important role in supporting microenterprises with know-how on tax returns which is important in the country's efforts to address the informal economy. The NGO sector also makes an important contribution to the knowledge and know-how effort. For example, in Armenia, a Junior Achievement initiative provides active support to schools on entrepreneurship promotion, with specific inputs into teacher training. However, a conditional feature of the indicator on non-formal entrepreneurial learning is that it should be supported by a working group as part of a strategy for lifelong entrepreneurial learning which all countries should work towards. The objective of a working group monitoring non-formal entrepreneurial learning developments is to provide an advisory support framework to ongoing developments; and to promote greater visibility and exchange. There are examples of this type of arrangement in other transition economies – and to good effect. Croatia's E4E (education for entrepreneurship) support framework, for example, is a good reference on how non-formal entrepreneurial learning developments feature alongside entrepreneurship promotion in the wider education and training system.

The assessment also focused on the role of the press in promoting awareness and understanding of the contribution of the non-formal training provider community to

entrepreneurial learning. What stands out in the assessment is the particular contribution of broadcasting media in the information-sharing drive. Armenia and Belarus, for example, have a range of TV programmes addressing small business development which include training, advisory and advocacy concerns. Azerbaijan also stands out for its more innovative approaches to the publicity drive (*e.g.* Internet television broadcasts on self-employment as a career option) and media coverage for specific segments of the SME market (*e.g.* television programmes for small farming businesses). Meanwhile, the Belarus press corps played a significant role in 2011 in disseminating information during the country's designated Year of Entrepreneurship.

Entrepreneurship promotion in upper secondary education well developed across the region

As a whole, the assessment of entrepreneurship promotion in upper secondary education is well developed in the region. An important factor has been the inclusion of entrepreneurship within the national curriculum framework in most countries.

Entrepreneurial learning in upper secondary education (ISCED 3)

The indicator requires that entrepreneurship is addressed at two levels within the curriculum: first, as a key competence and where entrepreneurship is embedded within the general curriculum; and second, as a specific subject and where entrepreneurship skills are developed, either as an integral part of the curriculum or as an elective subject. The evidence for the promotion of key competence in most countries is that it is invariably part of a wider range of subject areas (*e.g.* life skills or social sciences) and where issues related to entrepreneurship and a broader understanding of business and society are addressed.

Azerbaijan stands out as the only country in the region which has formally adopted the EU recommendations for key competences. This is an important achievement. While the roll-out of the revised curriculum is phased, the formal inclusion of the EU entrepreneurship key competence provisions in the curricula provides a sound basis for promoting the next entrepreneurial generation.

One feature of the assessment process has been the immediate response by the national authorities, in a number of instances, to the issues and findings from the assessment. The Republic of Moldova, for example, is finalising plans for the inclusion of a voluntary module for entrepreneurship in upper secondary education. Following the SBA recommendations, there is now an opportunity to give consideration to the entrepreneurship key competence in the wider curriculum and teacher training.

A more developed effort in all countries which singularly addresses entrepreneurship as a key competence will be important. This will require reflection on the definition of learning outcomes for the key competence, including implications for adjustments to the existing curriculum, teacher training and school governance arrangements. In this regard, the key competence developments in the countries of the Western Balkans and Turkey, co-ordinated by the South East European Centre for Entrepreneurial Learning (SEECEL), is a good practice reference point and where all countries are co-working the entrepreneurship key competence agenda.

Finally, a demanding feature of the indicator is ensuring evidence that the entrepreneurship features of the national curriculum are being delivered across the school

network. Armenia and Azerbaijan stand out particularly here where evidence forms part of learning plans and programmes for the schooling system. To move forward on the indicators in a subsequent SBA assessment other EaP countries will need to consider how the entrepreneurship agenda in the school environment will be monitored. Teaching plans are a good reference tool to measure progress.

Good policy awareness on women's entrepreneurship across the region

The assessment of women's entrepreneurship points to good policy awareness in all countries with examples of more developed policy provisions in a number of countries. Training and access to finance require more considered attention while improved advocacy arrangements will be important to a more sustained contribution of women entrepreneurs to the economy.

Policy support framework for promotion of women's entrepreneurship

A central feature of the women's entrepreneurship area within this SBA dimension is that development of women's entrepreneurship requires a comprehensive set of gender-sensitive policies. Women's entrepreneurship has no one policy home. For the effective promotion of women's entrepreneurship a range of policy areas need to be given equal consideration. These are economic, social, fiscal, education and employment policies. This makes for a complex policy paradigm but addressing all areas is important in creating the enabling environment which will allow women to join the entrepreneurship drive in each country.

The assessment finds that policy developments for women's entrepreneurship are most advanced in the Republic of Moldova and Georgia. In the Republic of Moldova, a National Programme for Gender Equality has brought together the range of policy concerns referred to above, while Georgia has already moved forward with an action plan for implementation of gender equality which gives particular emphasis to improved training and business support services for women entrepreneurs. The Republic of Moldova's efforts are reinforced with direct institutional support for a co-ordinated policy drive by the Ministry of the Economy while in Georgia a Gender Equality Advisory Council within the Parliament of Georgia oversees policy developments in this area.

Meanwhile, Armenia, Azerbaijan and the Republic of Moldova already have ongoing dialogue on the range of policy areas which support a sustainable women's entrepreneurship drive. The issues here need to be brought together within one policy framework if there is to be a serious and concerted effort by the countries to ensure that women contribute to a more competitive economy. In Belarus and Ukraine, the remnants of some former and excellent policy initiatives were evident through the assessment. What is clear is that the women's entrepreneurship policy should not be characterised as a gender issue which can easily be swept under the carpet upon a change of administration or other intervening factors. Women's entrepreneurship is an economic issue and must be firmly embedded in the country's drive for growth and competitiveness.

Apart from policy considerations, all countries demonstrate a range of support activities for women's entrepreneurship. The networks, energy and drive of those involved at the grass roots level to improve women's entrepreneurship should be harnessed. More developed networking, recognition and inputs into the policy process will be important.

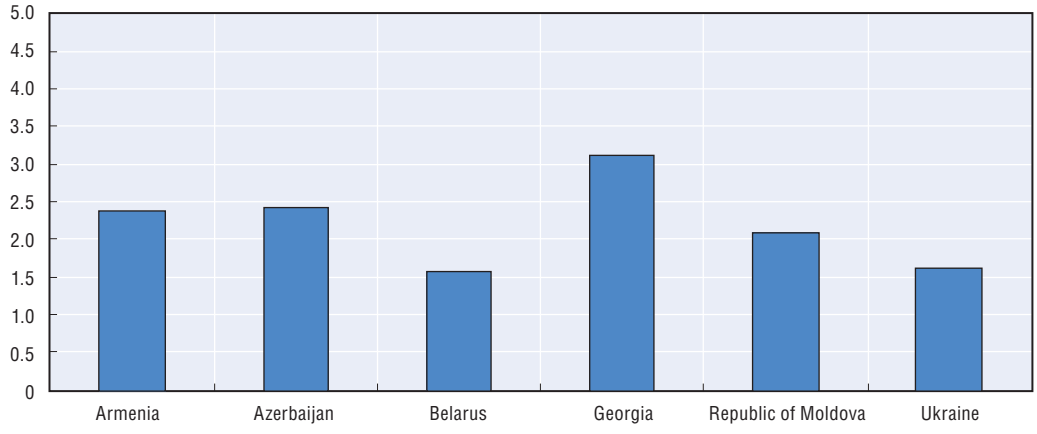
It will be crucial that all countries continue to raise the issue of women's entrepreneurship in broader development plans as a pre-condition for a more competitive economy and improved employment. Strong policy advocacy groups will be important here to ensure that the issue is sustained on the national policy agenda even with a change of administration. Finally, the evolving policy drive in the region should be accompanied by monitoring and evaluation with the objective of continuous improvement of initiatives and cost-effectiveness.

The way forward

Two proposals are provided below to bring forward developments in entrepreneurial learning and women's entrepreneurship:

- Given the newness of the entrepreneurship key competence agenda, many challenges remain across all countries in ensuring that the key competences are addressed effectively and are monitored. One way forward would be to borrow on the experience of the SEECEL open method of co-ordination. This would involve all countries co-working entrepreneurship key competence developments in terms of curriculum innovation and teacher development.
- Consideration should be given to building strong advocacy groups in each country with the objective of establishing a reference point for government on economic and social policy and where women's entrepreneurship would be promoted and sustained. The advocacy groups could borrow on the model of the EU women ambassadors networks which not only provide an excellent advocacy service in terms of policy, but which double up as service providers at the grassroots level to provide training and mentoring services and, just as important, to act as role models for women to take the business route.

Figure 3.2. **Weighted scores for Dimension 1: Entrepreneurial learning and women's entrepreneurship**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Notes

1. Iceland does not participate in the SBA assessment process.
2. All indicators (apart from the indicator for women's entrepreneurship policy) had already featured in previous assessments in the pre-accession region. The women's entrepreneurship indicator is a new addition to the SBA assessment framework. In 2011-12, the indicator was road tested for the first time in all EU pre-accession and Eastern Partner countries. The outcomes of the assessment in the pre-accession regions are covered in a separate report.
3. This framework definition was agreed by an international working group in Geneva on entrepreneurial learning on 18 January 2012. The working group comprises ETF, GIZ, ILO, UNESCO and UNEVOC.

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PART II

Chapter 4

Bankruptcy and second chance for SMEs (Dimension 2)

Ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance (Small Business Act Principle 2)

Efficient bankruptcy procedures are an important condition for facilitating exit and re-entry of businesses into the market. Dimension 2 of the Small Business Act addresses the need to implement well-structured bankruptcy laws and to simplify bankruptcy procedures. Moreover, it encourages governments in identifying the right approach to supporting market re-entry of honest entrepreneurs who have previously failed in their business activity.

The first part of this chapter assesses the efficiency of bankruptcy procedures in the Eastern Partner (EaP) countries based on the existing legal framework and performance indicators, such as the time required for completion of bankruptcy proceedings, the costs incurred and the rate (in %) claimants can recover from an insolvent firm. The second part focuses on the public policy approach to facilitate re-start by promoting a positive attitude, determining favourable discharge procedures, supporting debt settlement and avoiding discriminatory measures in access to support schemes or public procurement tenders.

Introduction

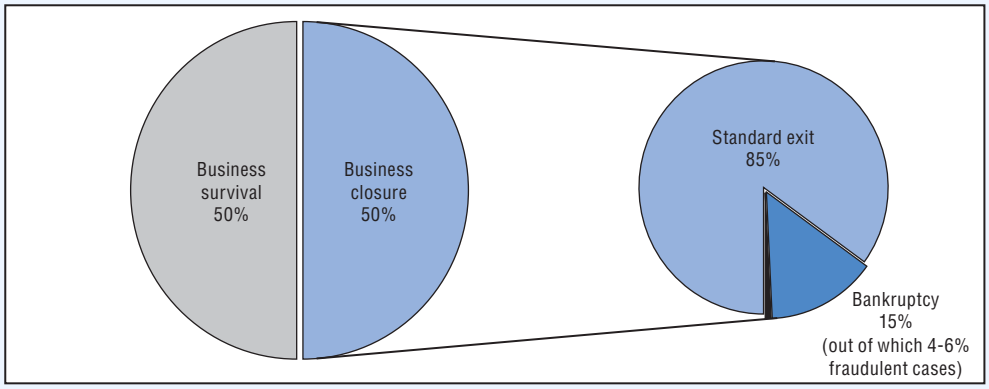
Business failure is considered a natural part of economic life which should be seen as an opportunity for a more re-invigorated re-start and future success (see Box 4.1). It is an integral part of the process of creative destruction which drives progress and economic growth. Thus governments should facilitate the restructuring or exit of insolvent companies that fail to fulfil their financial obligations and give entrepreneurs who have undergone non-fraudulent bankruptcy a second chance.

Box 4.1. **Business failure in the EU**

About 50% of companies in the EU close down within five years of start-up, 15% of these through bankruptcy procedures. However, only 4-6% of all bankruptcy cases are fraudulent which typically involves concealment of assets, fraudulent claims, false statements or other criminal acts depending on the jurisdiction. Nevertheless, public opinion stigmatises business failure as the broader public does not differentiate between honest failure and fraud. Would-be entrepreneurs are reluctant to start a business because they fear the negative consequences of business failure. Also, re-starting a business after failure is burdensome.

The stigma of business failure has a severe negative economic impact. According to estimates, 135 000 registered companies close down every year in the EU25 as a consequence and about 1.4 million jobs are lost in the EU15. On the other hand, businesses set up by re-starters often grow faster than businesses set up by first-timers and 18% of successful entrepreneurs in the EU have already run one enterprise. There is thus a strong rationale for public policy to act: *i)* to enable the completion of all legal procedures to wind up a business within a year; *ii)* to promote a positive attitude towards a fresh start; and *iii)* to ensure that re-starters are treated on an equal footing with start-ups.

Figure 4.1. **Business survival rates in the EU within 5 years of start up**



Source: European Commission (2011), Report of the Expert Group "A Second Chance for Entrepreneurs: Prevention of Bankruptcy, Simplification of Bankruptcy Procedures and Support for a Fresh Start", January 2011, OECD Analysis.

Bankruptcy is the legal status of insolvency determined by court order. It plays an important role in enabling the market to dispose of inefficient firms and re-allocate assets of insolvent debtors to more productive activities. To ensure a well functioning bankruptcy process, a first step is the systematic implementation of bankruptcy laws and procedures. Equally important is having well trained bankruptcy lawyers and specialised bankruptcy courts in place. Judging from both legal and economic reasoning, bankruptcy legislation should be designed so that it increases the efficiency of procedures while preserving the principles of fair and equal treatment of all parties involved in the re-organisation or liquidation process (Cabrillo and Depoorter, 2000).

Bankruptcy procedures should be designed in such a way that they reduce losses for all parties involved. Losses are typically incurred through inefficient proceedings that are lengthy and burdensome.

On the debtor's side, time spent in closing down a business creates high opportunity costs as time is lost which could be better spent in entrepreneurial activities. In addition, the longer the process takes, the higher the costs of court proceedings and the smaller the value of the remaining estate that could eventually be preserved. This further reduces the prospect of successful company re-organisation.

On the creditor's side, reduced net value of the estate also means a lower recovery rate on the investment. Moreover, keeping a financially distressed company alive as a "going concern" may often be perceived as the better option in terms of maximising asset value. It should thus be in the interest of all parties involved to reduce the time and cost of procedures and maximise the recovery rate for creditors by identifying whether re-organisation or liquidation and debt enforcement might be the best scenario.

Setting the right balance between the interests of debtors and creditors also depends on a country's level of economic development (Djankov *et al.*, 2008). In high-income countries, re-organisation of a company is the best option to maintain the activity of a bankrupt company and to maximise its prospects of debt recovery. In middle-income countries, however, such as in the Eastern Partner (EaP) region, a stronger focus should be placed on preserving the rights of creditors to facilitate the development of a sound and active credit market. Banks are more likely to provide financing to companies if there is a guarantee that, in case of default, bankruptcy procedures will allow them to regain their loans.

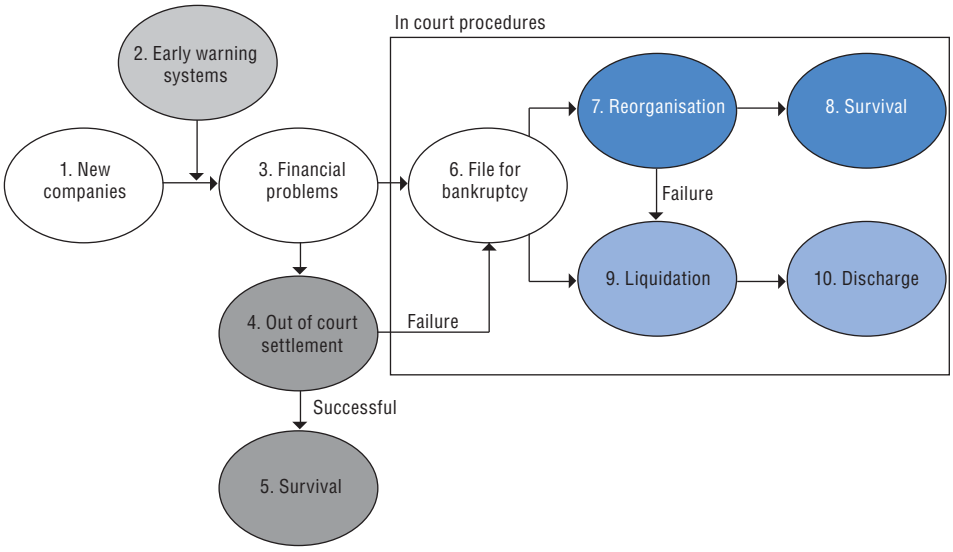
In general terms, a bankruptcy process can be divided into four consecutive sub-areas from the time a company starts experiencing financial problems until it is eventually reorganised or liquidated (OECD, 2006):

- As a first step, early-warning systems must be in place to identify financially distressed companies at a stage where providing additional support might help avoid filing for bankruptcy. Entrepreneurs will often not act on time and seek help only when there are no more alternatives for fear to lose control over their company. Seeking support means admitting defeat and questioning their entrepreneurial capacity.
- In a second step, out-of-court settlements should be available as a less expensive and less burdensome alternative to filing bankruptcy, especially for microcompanies. A necessary condition, however, is that all creditors must agree to keep the company alive. They must be assured that their rights are adequately secured during the entire process.
- Court procedures are the right option if neither step has been successful. Both creditors and debtors have the right to file for bankruptcy. This includes drafting a re-organisation plan and allowing the discharge of part of the debt through court ruling, leading either

to the re-organisation and survival of the company or to its liquidation. Once started, bankruptcy proceedings should be fast and cost-efficient so that a reasonable proportion of the assets can be saved and any potential re-start will not be overly delayed.

- Post-bankruptcy treatment including liquidation, discharge and its consequences should be structured in a non-discriminatory manner. This enables the entrepreneur to achieve a quick re-start. Long debt repayments, a lack of discharge or non-automatic removal from bankruptcy registers and national credit rating black lists can prevent an entrepreneur from accessing the finance needed for a second chance.

Figure 4.2. **Example of bankruptcy process design**

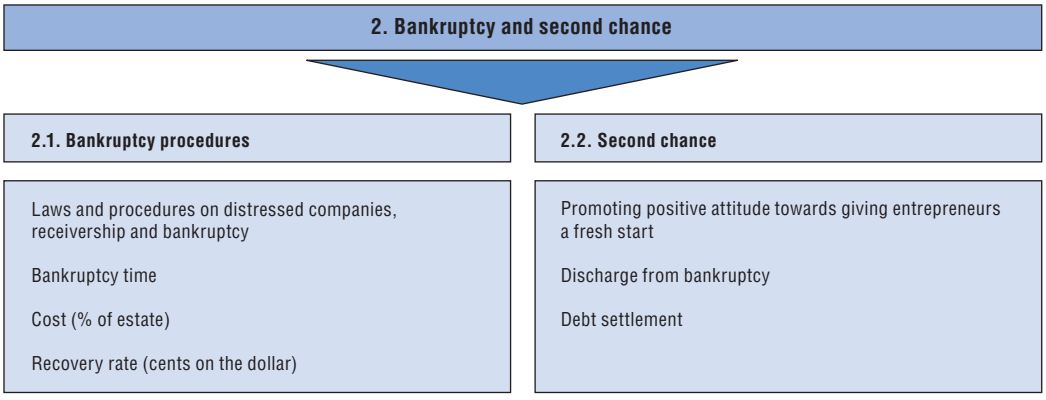


Source: OECD (2006) and CFE/SME (2006)3, *Entrepreneurship Policy Indicators for Bankruptcy Legislation in OECD Member and Non-member Economies*, OECD, Paris; CFE/SME Secretariat.

Assessment framework

The assessment of Dimension 2 is structured around two sub-dimensions: Bankruptcy procedures and second chance (see Figure 4.3 below).

Figure 4.3. **Assessment framework for Dimension 2: Bankruptcy and second chance**



Bankruptcy procedures

The first sub-dimension measures the sophistication of bankruptcy laws and procedures by looking both at legislation and administrative practice. The first indicator in this sub-dimension measures the existence of laws and procedures on distressed companies, receivership and bankruptcy as well as their compliance with international standards. To fulfil these standards, bankruptcy legislation must reconcile the conflicting interests of creditors (banks, suppliers, customers, employees) and debtors (entrepreneurs, companies) who fail to fulfil their financial obligations. Creditors' interests must be protected while viable companies should be kept alive. The role of public policy is to strike the right balance between these parties. It must provide an efficient mechanism and judicial system to ensure rapid re-organisation and survival of viable companies or the proper liquidation and structured redistribution of company assets and property of those that are not viable.

The indicators bankruptcy time, cost (% of estate) and recovery rate (cents on the dollar) are measured by the World Bank's *Doing Business 2012* report (resolving insolvency) and help to reveal weaknesses, particularly as pertains to the legal application such as procedural and administrative bottlenecks in the bankruptcy process and a limited capacity or complete lack of specialised courts or trustees to deal with them.

Second chance

The second sub-dimension looks at the measures in place to facilitate the second chance for entrepreneurs and to reduce stigmatisation of business failure. To achieve this objective, public policy should minimise the economic impact of lost entrepreneurial potential stemming from discriminating treatment of entrepreneurs who have undergone bankruptcy and who are suffering the stigma of business failure. This can be achieved through promotional campaigns and by reducing the barriers for potential re-starters in starting a new business.

The concept of giving honest entrepreneurs a second chance is based on the notion that bankruptcy cases should be seen as a learning experience for an entrepreneur rather than the entrepreneur being stigmatised or penalised. Research shows that businesses set up by re-starters grow faster and create more jobs and turnover than first-timers (Stam, Audretsch and Meijaard, 2006). Nevertheless, it is important to systematically distinguish between honest but unlucky entrepreneurs and those who have undergone fraudulent bankruptcy. While the former group should be encouraged to undertake a fresh start, effective measures must be taken to prosecute wrong-doers (European Commission, 2011).

Several mechanisms for public policy can promote a second chance and encourage honest entrepreneurs to re-start. This report measures three elements: *i)* promoting a positive attitude towards giving entrepreneurs a second chance; *ii)* discharge procedures; and *iii)* the role of public authorities in supporting a quicker debt settlement:

i) *Promoting a positive attitude towards giving entrepreneurs a fresh start.* Public administrations can play an active role in encouraging potential re-starters through training and information campaigns on second chance. In addition to providing targeted support measures, an effective second chance policy should send the message that entrepreneurship may not end up as a "life sentence" in case things go wrong (European Commission, 2011).

ii) *Discharge from bankruptcy.* Including discharge procedures in bankruptcy laws and/or procedures is an important mechanism to release an entrepreneur from pre-bankruptcy debt within a given time frame after a final court decision. The European Commission recommends a delay of three years which should be accompanied by removal from bankruptcy registers and national credit rating black lists.

iii) *The role of public authorities in supporting a quicker debt settlement.* Public authorities can play a supporting role if tax debts take lowest priority over any other debt in a bankruptcy (except social security contributions which should come first). Giving preferential treatment to both secured and unsecured creditors is also an important element to support a functioning credit system and the supply of external financing.

A study conducted by Armour and Cumming (2005) provides empirical evidence on the economic effect of bankruptcy laws on self-employment rates in 15 countries. It shows that a non-discriminatory approach towards giving entrepreneurs a fresh start can promote entrepreneurship and encourage risk taking. As an example, the authors find that reducing the discharge time of a pre-bankruptcy debt by 10 years is likely to result in an increase in self-employment by approximately 1.5% (Armour and Cumming, 2005). Hence, a bankruptcy law which is more forgiving is likely to result in higher levels of entrepreneurship.

Analysis

EaP countries need to introduce more streamlined systems to deal with bankruptcy cases and reduce the time and cost of proceedings

In all EaP countries, laws and procedures concerning distressed companies, receivership and bankruptcy are in place. However, the level of sophistication varies especially with regards to commencement provisions, avoidance of pre-bankruptcy transactions and provisions relating to re-organisation proceedings. These can be used, among other indicators, as a proxy to assess compliance of bankruptcy legislation and procedures with international standards.

The EBRD *Insolvency Law Assessment* carried out in 2009 provides detailed analysis of insolvency proceedings across the region (EBRD, 2009). Based on these results, EaP countries can be classified into two groups. Armenia, Belarus and the Republic of Moldova were rated as having "medium compliance" whereas Azerbaijan, Georgia and Ukraine only received a "low compliance" rating with regards to international standards:

- The first group of countries ("medium compliance") is performing well, particularly as regards commencement provisions and dealing with creditors. Both Belarus and the Republic of Moldova also have strong provisions relating to the avoidance of pre-bankruptcy transactions, a point that requires improvement in the case of Armenia. On the other hand, re-organisation proceedings are well established in Armenia but remain weak in Belarus and the Republic of Moldova, given that there are no provisions for the independent analysis of a proposed plan of re-organisation. In addition, in the case of Belarus, special conditions apply to state-owned companies. These can only be financially rehabilitated and not liquidated.
- In the second group of countries ("low compliance"), basic international standards have not yet been achieved. Bankruptcy laws in Azerbaijan, Georgia and Ukraine remain weak mostly as regards commencement provisions (no provision for balance sheet insolvency test), pre-bankruptcy avoidance provisions and re-organisation proceedings, among other issues. Amendments to the current laws are required to increase the level of compliance.

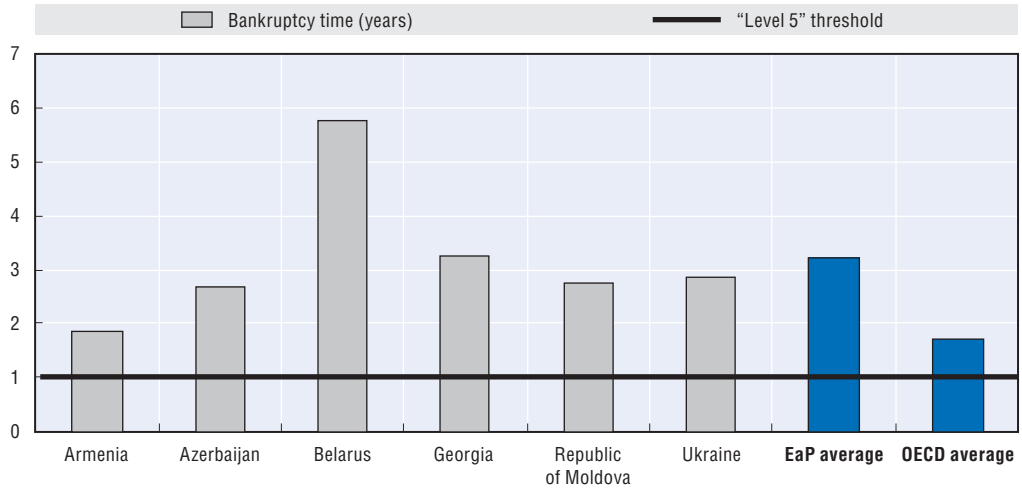
There are also significant differences across the EaP region as to the bankruptcy time (years) required to close a business, the cost (% of estate) incurred and the recovery rate (cents on the dollar) that creditors can expect to obtain from bankruptcy cases.

As a best practice threshold to attain a "Level 5" ranking, this report considers a bankruptcy time of no longer than one year as desirable, the maximum cost of bankruptcy proceedings as 8% of the estate's value and a minimum recovery rate of 70 cents on the dollar that claimants can recover from an insolvent firm through re-organisation, liquidation or debt enforcement.

With regards to bankruptcy time required and cost incurred, EaP countries can again be divided into two groups:

- Armenia, Azerbaijan, Georgia and the Republic of Moldova are performing above average. All four countries show indicators close to or below the EaP average of 3.2 years spent and 14.8% of cost as a percentage of the estate's value incurred through the proceedings. In Georgia bankruptcy time has been further reduced through recent amendments to the law.
- Belarus and Ukraine, on the other hand, perform far below the EaP average in at least one of the two categories. In Ukraine, bankruptcy time takes a relatively moderate 2.9 years but the cost incurred is as high as 42% of the estate. In Belarus, both the cost incurred is high (22% of the estate) and the average time spent in court procedures is excessively long (5.8 years). In both countries, it is therefore unlikely that a company undergoing bankruptcy procedures will have a chance for re-organisation.

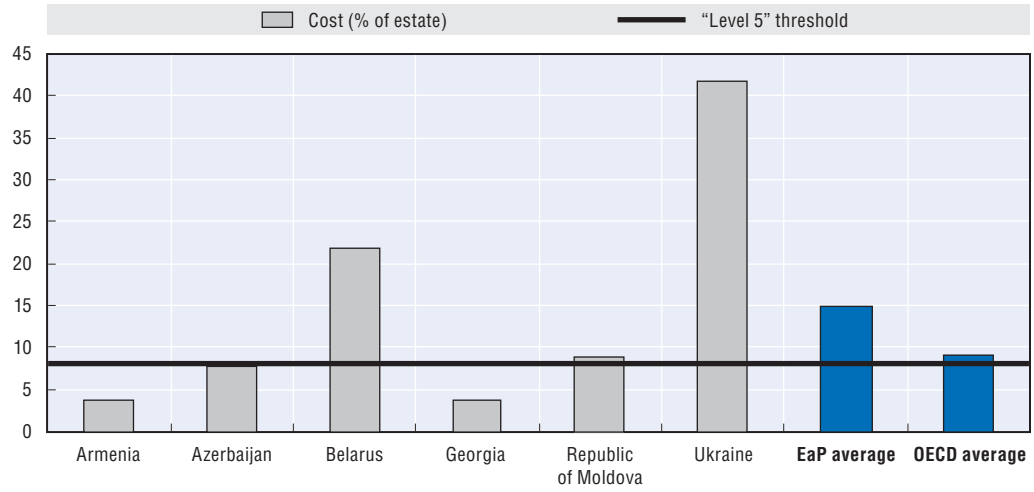
Figure 4.4. **Bankruptcy time (years)**



Source: World Bank (2012), *Doing Business 2012*.

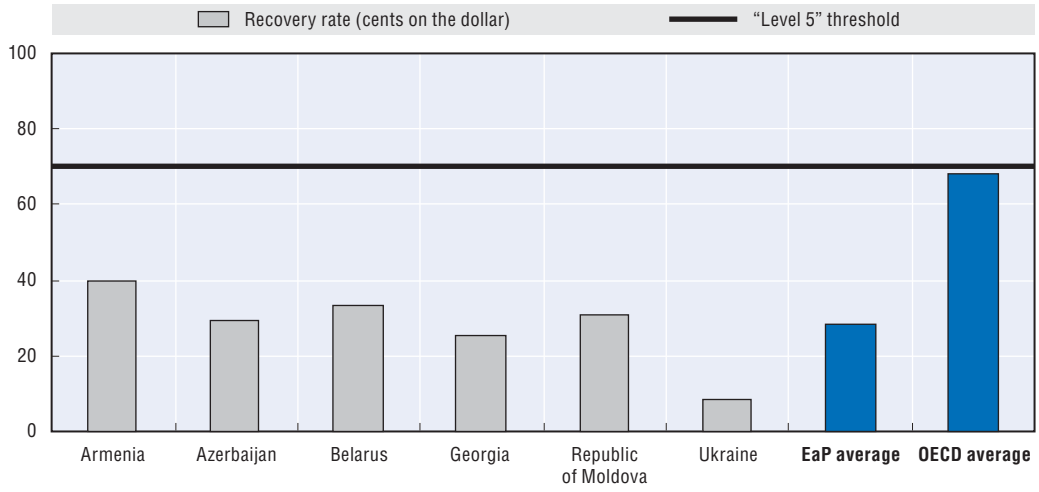
Despite these significant differences in the time and cost of proceedings across EaP countries, it should be noted that the recovery rate is equally low across the entire region. In none of the countries can creditors expect to receive more than 40% of their claims through formal bankruptcy procedures. This is low in comparison to the OECD average of 69.1%. This result can largely be traced back to both deficiencies in the bankruptcy laws and their application, leading to the high cost of proceedings and/or making it often too easy for debtors to commit bankruptcy fraud such as concealment of assets or pre-bankruptcy transactions.

Figure 4.5. **Bankruptcy cost (% of the estate)**



Source: World Bank (2012), *Doing Business 2012*.

Figure 4.6. **Bankruptcy recovery rate (cents on the dollar)**



Source: World Bank (2012), *Doing Business 2012*.

Table 4.1. **Scores for sub-Dimension 2.1: Bankruptcy procedures**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
2.1.1.	Laws and procedures on distressed companies, receivership and bankruptcy	4	3	3	3	3.5	3
2.1.2.	Bankruptcy time (DB indicator)	4	3	1	2	3	3
2.1.3.	Cost (% of the estate) (DB indicator)	5	5	2	5	4	1
2.1.4.	Recovery rate (cents on the dollar) (DB indicator)	3	2	2	2	2	1
Weighted average		***4.00***	***3.25***	***2.00***	***3.00***	***3.13***	***2.00***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

EaP countries could play a more proactive role in supporting honest re-starters

Specific information campaigns on second chance are not being conducted by public administrations in any EaP country. There is also no evidence of training to target honest entrepreneurs who have undergone non-fraudulent bankruptcy and are seeking support for a successful re-start. This is not surprising given that the second chance policy is a rather new concept in the European Union as well. Since 2007, the European Commission has invited member states to facilitate a second chance and to act to reduce stigmatisation of business failure (European Commission, 2007).

So far, only Belarus has established formal discharge procedures for debts and liabilities on completion of proceedings. Within ten days after a liquidation decision is taken a liquidation entry is made in the Uniform State Register of Legal Entities and Individual Entrepreneurs after which the debtor is deemed liquidated if it is a legal entity or free of debts if it is an individual entrepreneur. In the case of Ukraine, the establishment of discharge procedures is currently under consideration in combination with the formation of a unified national register for legal entities under bankruptcy procedures. In all other countries, discharge procedures are not determined by law. In the case of Armenia, the law gives a clear indication of those liabilities that a debtor may not be declared exempt from. In the case of the Republic of Moldova, creditors are free to pursue the debtor after cessation of insolvency without any limitation. There are no specific regulations in the laws of Azerbaijan and Georgia. In Georgia, specific discharge procedures are not stipulated in the Law on "Insolvency Proceedings" (2007), however, according to the Georgian government, discharge from debt is automatic consequence of finalisation of insolvency proceedings and removal from the business registry.

With regards to the role of public authorities in supporting a quicker debt settlement, none of the EaP countries gives lowest priority to tax debts which would be desirable:

- The most favourable regulations from a creditor's perspective are in Armenia, Georgia and Ukraine where some tax concepts take lower priority over other debts and secured creditors can expect to be treated preferentially. However, it should be noted that in Georgia, recent changes to the tax code have strengthened the position of tax authorities over unsecured creditors. Also, in Ukraine, even though by law secured creditors take higher priority, given the low recovery rate (8.9%), the current system does not provide for quick and effective liquidation of insolvent companies.
- In Azerbaijan, Belarus and the Republic of Moldova regulations are less favourable. In Belarus, tax debts do not take first priority but are compensated even before secured creditors. In Azerbaijan and the Republic of Moldova all tax debts take first priority; payment by instalments is available in the case of the Republic of Moldova.

Table 4.2. **Scores for sub-Dimension 2.2: Second chance**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
2.2.1.	Promoting positive attitude towards giving entrepreneurs a fresh start	1	1	1	1	1	1
2.2.2.	Discharge from bankruptcy	1	1	4	5	1	2
2.2.3.	Debt settlement	2.5	1	2	2.5	2	2.5
Weighted average		***1.50***	***1.00***	***2.33***	***2.83***	***1.33***	***1.83***

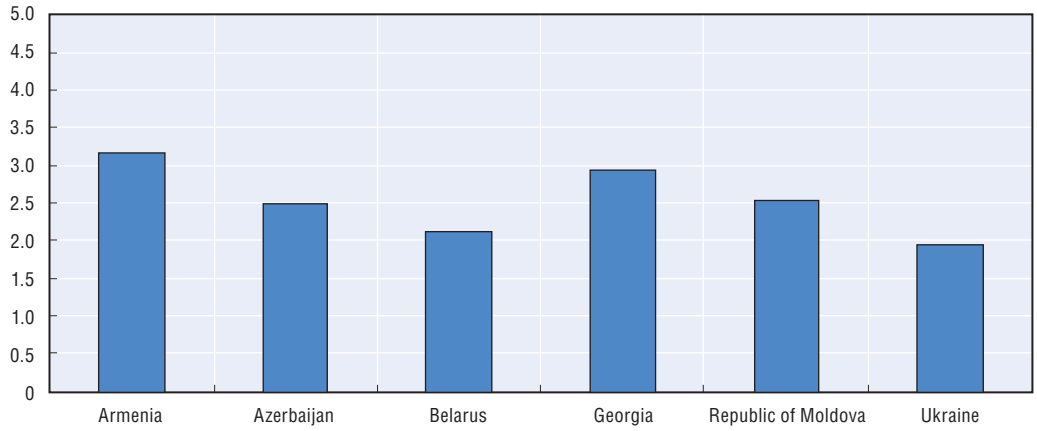
Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

Overall, EaP countries should further reform their existing bankruptcy legislation to include provisions on commencement, avoidance of pre-bankruptcy transactions and provisions relating to re-organisation proceedings. In order to improve the efficiency of the process, reforms should be implemented to reduce delays which would also have a positive effect on the cost of proceedings and the recovery rate of the debt. Measures should also be taken to ensure that bankruptcy cases are dealt with by specialised courts and that judges and officials in charge of administrating insolvency cases have received sufficient training. Furthermore, EaP countries would benefit from formally regulating out-of-court settlement as an instrument to foster cost-effective management of insolvency processes.

In applying a second chance policy, EaP countries would benefit from introducing specific regulations dealing with aspects of facilitating a re-start, such as clearly establishing discharge procedures in their legislative framework. To strengthen creditors' rights, it would also be advisable to establish bankruptcy registers which would provide information on businesses currently undergoing bankruptcy procedures. Nevertheless, after full discharge, automatic removal from such registers should be possible within a maximum of one year.

Figure 4.7. **Weighted scores for Dimension 2: Bankruptcy and second chance**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 5

Regulatory framework for SME policy making (Dimension 3)

Design rules according to the "think small first" principle
(Small Business Act Principle 3)

The "think small first" principle of the Small Business Act requires full consideration of SMEs at an early stage of policy development. The capacity to create and implement effective public policy is determined by the structure of the process and its ability to promote timely and appropriate regulation. A policy and institutional framework to tackle SME needs is an important first step to creating a favourable business environment for SMEs. This chapter focuses on the institutional framework for SME policy making and provides an overview of the institutional framework set in place in the Eastern Partner (EaP) countries. It describes three aspects of the SME policy process: the institutional framework, legislative simplification and regulatory impact analysis (RIA) and public-private consultations.

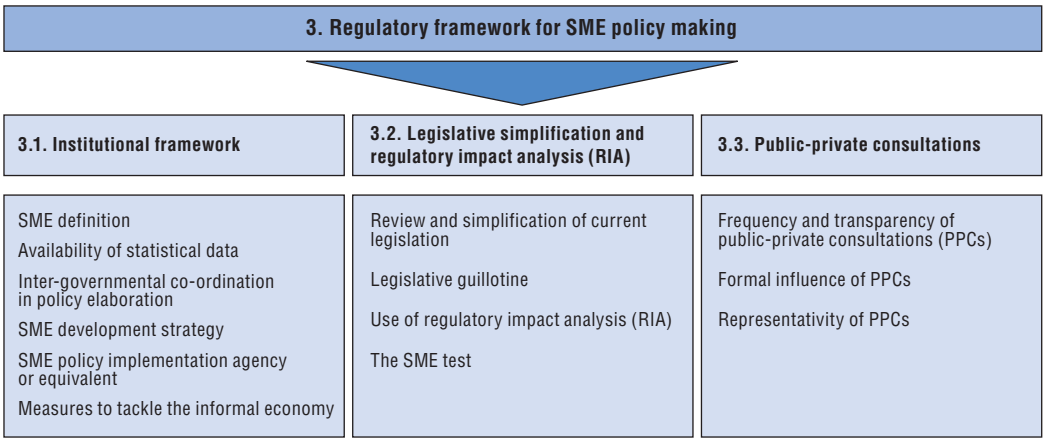
Introduction

The "think small first" principle requires that the interests of SMEs are taken into account at an early stage of policy making. Given that SMEs represent the largest share of companies in most economies, SME-friendly institutions and legislation, as well as regular consultations with the private sector, which give full consideration to the specific needs of small and medium-sized companies, are an important pre-condition to a favourable business environment.

Assessment framework

The assessment framework of the principle/dimension is composed of three sub-dimensions, analysing three different aspects:

Figure 5.1. **Assessment framework for Dimension 3: Regulatory framework for SME policy making**



Institutional framework

The first sub-dimension assesses the level of development of the institutional framework. The sub-dimension includes a range of indicators starting from the definition of the SME sector as the target group, to the governmental institutions that regulate the SME policy. Having a policy and institutional framework to tackle SME needs is an important first step towards creating a favourable business environment in which SMEs can thrive. The way the institutional framework is designed plays an important role in how effectively the policy, and in this particular case the SME policy, is developed and implemented. Having clear and well-defined responsibilities and tasks for government institutions that are involved in the different stages of SME policy making is one of the pre-conditions for the creation and adoption of high quality regulation.

SME definition

As a first step towards an effective institutional framework, it is important to recognise small business as a target group, and therefore define it. Ideally, one single definition should be used across all legislation, in order to ensure a common view on what SMEs represent in a country. Furthermore, synchronising the definitions across countries allows international comparison and exchange of best practice, as in the case of the EU countries that are now using one single definition (see Table 1.3).

Availability of statistical data

Availability of statistical data is also crucial for targeted policy making. The accessibility of accurate, up-to-date, detailed data allows the policy maker to make an accurate assessment of the current situation of SMEs, and develop relevant and targeted solutions to the existing problems. Moreover, given that the information may also be used by the SMEs (which generally have fewer capabilities to generate this type of information internally compared to large firms) to detect market and sector trends. This, in turn, may help them make the right decisions and increase their competitiveness in the market.

Inter-governmental co-ordination in SME policy elaboration

As SME policy touches upon a wide range of issues, such as innovation, agriculture, science, education, etc., an increasing number of institutions are involved in the implementation of parts of SME policy. Given this complex nature of the policy-making process, a successful and effective policy would almost always include a co-ordinating body, with a meaningful mandate to ensure effective communication and co-ordination (OECD, 2011c) that would be in charge of mediation between the relevant institutions. The co-ordination will allow these policy areas to be seen as components of a system rather than separate policy areas for which different ministries are responsible (see Box 5.2 for a relevant example). The co-ordinating body may take the form of an inter-ministerial committee, or a specialised SME development department that can ensure liaison with all the relevant ministries and government bodies.

SME development strategy

To ensure that the decisions on an array of policies are seen as an end-to-end process, the government should take a strategic approach to policy making. This means that policies should be developed within the framework of a longer-term strategy. Policy making as such involves many stakeholders, policy instruments and initiatives that are not always coherent, may have overlaps or even pursue contradictory targets. The value of a strategy thus lies in its ability to link all the elements of a policy-making process and define common goals. The absence of such a strategy may lead to a fragmented policy, non-co-ordinated actions and random solutions to existing problems.

The strategy should be based on a clear understanding of the situation of SMEs in the country, backed up by strong evidence (statistics, surveys, etc.). It should be reactive to the changing environment and needs of the SME sector. At all stages of strategy development, financial and time constraints should be taken into account. Overambitious initiatives risk not being implemented. Most importantly, the strategy should be politically approved and followed. As such, all the institutions involved should be informed about their role, while its message has to be clearly communicated to the private sector so that everybody can

strive towards these goals. To sum up, an efficient policy strategy will have the following characteristics (*Strategy Survival Guide*, 2004):

- Suitability – clear objectives, backed up by evidence, causes and possible future scenarios; flexible and adaptable to changing circumstances.
- Feasibility – based on a strong evidence base, as well as a realistic understanding of the effectiveness and costs of different policy instruments and measures envisaged.
- Acceptability – the strategy needs to have sufficient political and public support; it should be developed and communicated effectively to the public.

Having a strategy for SME development brings a variety of benefits. First of all, a strategy allows positioning of SME development targets within the framework of the larger national economic and social goals, such as poverty reduction, job creation, integration of specific groups into the national entrepreneurial culture, etc. It also allows harmonisation of national, regional and local efforts for SME development. The strategy can also be a tool for monitoring progress in the SME sector over time, as well as being a reference point for communication and debate with different stakeholders on policy impact, progress achieved and future goals.

SME policy implementation agency or equivalent

An SME policy implementation agency, with a clear mandate of authority, would finally translate the goals and objectives of the SME strategy and the resulting policies into operational programmes. The agency would be responsible for the translation of policy goals into operational rules and development of guidelines for the programme, as well as the co-ordination of resources and personnel to achieve the intended goals. The implementing agency could be a special department in the Ministry of Economy, or an independent or an autonomous state agency. Most importantly it has to be separate from the body developing the policy and monitoring its implementation to ensure the accountability and transparency of the process. At the same time, full political support is crucial for its effective operation as this would eventually translate in adequate funding and staffing for the implementation of the actions envisaged in the SME policy action plans.

The SME implementation body does not have to be the actual implementer of all the final services. Major forms of support can be outsourced to private sector representatives, NGOs or financial institutions, for example training, consulting, incubation, financing, etc. Outsourcing is particularly useful if the national agency does not have the capabilities or sufficient geographical outreach to cover a wide range of SMEs.

Measures to tackle the informal economy

Given that regulatory constraints represent a bigger burden for microfirms than for their larger peers, the incidence of informality tends to decrease as the size of the firm increases. Due to this informality a large and important part of the target group for SME policy is not on the radar of policy makers. Even though informality often results in increased (informal) employment, it has a number of negative effects:

- The budget revenue, and hence the availability of funds for further SME support, is reduced.
- Competition on the market is distorted to the detriment of firms operating formally, thus pushing them into the informal sector as well.

- Employees functioning informally do not benefit from social security and medical insurance.
- Firms operating informally are less likely to benefit from state support, as they are not registered and therefore more reluctant to co-operate with state institutions.
- Finally, the presence of a large informal sector distorts official statistics and hence may affect policy decisions away from optimal solutions.

Creating conditions that would provide benefits to the firms operating formally, instead of penalising them, is an important step towards formalising the entire economy and providing access to all the firms that need further state support. In this regard, taking a strategic approach, with clear responsibilities and targets, can ensure the achievement of the set objectives in a timely and efficient manner.

Legislative simplification and regulatory impact analysis (RIA)

The second sub-dimension assesses the mechanisms for legislative simplification and implementation of RIA and SME test. Managing the regulatory environment is an important aspect of the regulatory framework, allowing the government to keep policy making under control and not overburden the economic environment with laws and regulations. RIA in particular refers to a process of systematically evaluating the costs, benefits and social impacts that may arise from the adoption of new legislation or regulations. The aim of RIA is to improve and simplify the regulatory environment and ensure consistency amongst different policies.

It is crucial to consider SMEs when undertaking an impact assessment. The European Commission has developed specific guidelines for policymakers to conduct the "SME test" during RIA. The process includes the following steps (European Commission, 2009):

1. Consultation with SME representatives – this may involve roundtable discussions with stakeholders, test panels of entrepreneurs, specific committees or online consultations.
2. A preliminary assessment of the businesses likely to be affected – this involves an analysis of the number of businesses, proportion of SMEs, sectors and proportion of employment likely to be affected.
3. Measurement of the impact on SMEs – policy makers should conduct a qualitative and (where possible) quantitative assessment of the financial, substantive and administrative costs for SMEs resulting from the proposed legislation.
4. An assessment of alternative options and mitigating measures – this may be necessary particularly when the analysis indicates that SMEs are disproportionally affected or disadvantaged by the new legislation when compared to large companies.

Public-private consultations

Finally, the third sub-dimension analyses the frequency, transparency, formal influence and inclusiveness of consultations between the public and private sectors. Given that small firms are less organised and their needs much more diverse, their voice is often not heard when it comes to policy development (European Commission, 2005). The government therefore should always be in dialogue with the SME sector through institutionalised public-private consultations so as to be aware of its needs and challenges. Better communication will eventually lead to a bottom-up approach, with reforms that are solving the real problems of the private sector.

Ideally, the consultations should take place at all stages of policy making – starting from the initiation of discussion on potential legislation and drafting to evaluating the results and outcomes of a certain policy. The communication should be both reactive, providing policy feedback to the government, and pro-active, providing policy input to the government. Civil society, business communities and regular citizens should all be actively involved in the process (OECD, 2009). These consultations could be structured around the issue of SME development in general or focus on constraints faced by SMEs in key business sectors for SME growth (OECD, 2012b).

Two aspects must be considered when analysing public-private dialogue. The first is the formalisation and institutionalisation of public-private consultations, which will ensure that the dialogue is continuous and does not depend on the *ad hoc* decisions of policy-makers or changes in the political environment. The second is the effectiveness of consultations. This aspect is less tangible and more difficult to assess. Effectiveness often depends on the operational and organisational sides of the consultation, such as their frequency, format (debate, roundtable, etc.), representation of small business at meetings, early notice of meetings and preliminary distribution of relevant documents, etc.

Analysis

Building a strong institutional framework

The institutional framework encompasses many aspects of the policy-making process, from a definition of the SME sector as the target group, to establishment of institutions responsible for co-ordinating the policy. Table 5.2 lists the indicators of the sub-Dimension 3.1 that are used to assess the institutional framework in the Eastern Partner (EaP) countries, based on the EU Small Business Act.

Among EaP countries, Armenia and the Republic of Moldova already have the main building blocks for an SME policy in place. Georgia has made significant achievements by following a horizontal approach to business climate development, with relatively effective consultations and intra-governmental co-ordination mechanisms in place. In Ukraine, a new agency responsible for SME policy has been established in March 2012, but its effectiveness will largely depend on its mandate and financing. In Azerbaijan and Belarus, institutions in charge of SME policy development are currently at an early stage of development.

SME definition

In the EaP region, each country has a different definition for the SME sector, in most cases the key criterion for classification being the number of employees. Other criteria, such as turnover and total assets may also apply. Moreover, classification may also differ by sector, as in the case of Azerbaijan, reflecting structural differences between capital-intensive and labour-intensive industries.

Among the six EaP countries, only Armenia and the Republic of Moldova have definitions that consider the three criteria used by the EU countries – employment, turnover and total assets (in Armenia this definition is in force only since 1 January 2011). In Georgia and Ukraine the definition is based on employment and turnover, while in Belarus, according to the new definition adopted in 2010, "small business units" are defined based on the number of employees only. In Azerbaijan, apart from employment and turnover, definitions vary by type of activity (see Table 5.1 for more details).

Table 5.1. **SME definitions in EaP countries**

	Micro	Small	Medium	Large	*Source*
Armenia	Less than 10 employees; sales and assets less than AMD 100 million (~ EUR 0.2 m).	Less than 50 employees; sales and assets less than AMD 500 million (~ EUR 1 m).	Less than 250 employees; sales less than AMD 1 500 million (~ EUR 3 m) and assets less than AMD 1 000 million (~ EUR 2 m).	Firms that are not included in the definition of micro, small or medium enterprises.	Amendments from 5 October 2010 to the Law of the Republic of Armenia "On State Support of Small and Medium Entrepreneurship", in force since 1 January 2011.
Azerbaijan	Less than 50 employees and less than AZN 500 000 (~ EUR 0.5 m) turnover for construction and industry. Less than 25 employees and less than AZN 250 000 (~ EUR 0.25 m) for agriculture. Less than 15 employees and less than AZN 1 000 000 (~ EUR 1 m) for wholesale trade. Less than 10 employees and less than AZN 250 000 (~ EUR 0.25 m) for other sectors.			Firms that are not included in the definition of "small business units".	Decision of the Cabinet of Ministers of the Republic of Azerbaijan, from 18 December 2009.
	Turnover less than AZN 150 000 (~ EUR 0.15 m). Turnover less than AZN 120 000 for individual entrepreneurs.				Ministry of Taxes.
Belarus	Up to 15 employees.	16-100 employees.	101-250 employees.	Firms that are not included in the definition of micro, small and medium businesses.	Law of the Republic of Belarus of 1 July 2010, No. 148-3I, "On State Support for Small and Medium Entrepreneurship".
Georgia	Up to 20 employees and up to GEL 500 000 (~ EUR 0.23 m) turnover.		Up to 100 employees and up to GEL 1 500 000 (~ EUR 0.68 m) turnover.	Firms that are not included in the definition of small or medium enterprises.	Law of Georgia on "Georgian National Investment Agency".
	Annual turnover less than GEL 30 000 (~ EUR 13.5 thousand).	Annual turnover less than GEL 100 000 (~ EUR 45 thousand).			Georgian Tax Code, in force since 1 January 2011.
Republic of Moldova	Up to 10 employees, MDL 3 million (~ EUR 0.2 m) turnover and total assets.	Up to 50 employees, MDL 25 million turnover (~ EUR 1.6 m) and total assets.	Up to 250 employees, MDL 50 million (~ EUR 3.2 m) turnover and total assets.	Firms that are not included in the definition of micro, small or medium enterprises.	Law 206-XVI (2006) on Support of Small and Medium Sized Enterprises; National Statistical Bureau of the Republic of Moldova.
Ukraine	Up to 10 employees and up to EUR 2 million turnover.	Up to 50 employees and up to EUR 10 million turnover.	Firms that are not included in the definition of micro, small and large entrepreneurship.	More than 250 employees and more than EUR 50 million turnover.	Law of Ukraine, No. 4618-VI, from 22 March 2012 on "State Support of Small and Medium Entrepreneurship in Ukraine".

Note: Conversion of local currencies is approximate, based on the exchange rate of 7 December 2011.

While it is quite reasonable for the definition to differ across countries, due to the different economic conditions, it is important that the same definition is used across institutions. This is the case for all EaP countries except Azerbaijan and Georgia, where different definitions are used for statistical and tax purposes. This may create difficulties in assessing the impact of tax incentives for SMEs based on statistical data.

Availability of statistics

All EaP countries have a specialised institution which is responsible for collecting national and regional statistical data. Nonetheless, the data on the SME sector is often incomplete or entirely lacking. Georgia and the Republic of Moldova have the most comprehensive statistical websites with a large range of data on SMEs that is available online. The range of accessible statistical data is very wide, including information such as the contribution of the SME sector to the GDP, exports and investments, and is broken down both by region and by economic sector. Belarus publishes annual reports on the activities of small and medium enterprises and also covers a wide range of indicators.

In Armenia, Azerbaijan and Ukraine official data on the SME sector are very limited and fragmented. For example, the official statistical data cover only a limited number of sectors and exclude many small firms which are not in the monitoring database. The main

data for SME statistics are provided by the SME Development National Centre. The information is provided in a booklet and is based mainly on secondary data analysis, the key sources being several government institutions (National Statistical Service, State Property Management Department, Tax Service, etc.) as well as other formal and informal information sources. In Azerbaijan, general information can be found on the websites of various government bodies, and some basic statistical data (number, employment, output, etc.) on the official website of the State Statistical Committee of the Republic of Azerbaijan. In Ukraine, basic indicators are available, but there is no information on GDP.

While countries have made significant progress in recent years with regard to data collection and reporting, several important shortcomings remain to be addressed:

- Weak international comparability.
- Low accessibility and low level of detail.
- Limited availability online and lack of regular updates.

Collecting more detailed structural statistics and assessing the performance of the SME sector by carrying out regular surveys on active companies and collecting comparable data based on international statistical methodologies is crucial for informed fact-based policy making. Governments are particularly encouraged to look into the Eurostat methodology for measuring entrepreneurship (see Box 5.1 for more information) and the OECD Scoreboard on Financing SMEs and Entrepreneurs (OECD, 2012a).

Box 5.1. **The OECD-Eurostat Entrepreneurship Indicators Programme (EIP)**

The OECD-Eurostat EIP develops measures of internationally comparable data on entrepreneurial activity in 18 OECD countries, to provide a solid foundation for policy formulation and monitoring in this area. The measures are based on information produced by national statistical offices according to internationally agreed definitions. Policy makers and citizens alike can measure their countries' entrepreneurial performance, and compare it with other countries. The first data digests were published in 2008 and 2009 *Measuring Entrepreneurship* and in OECD (2011) *Entrepreneurship at a Glance 2011*. It can be considered a best practice and a successful attempt to synchronise the various definitions and statistics in the OECD countries and to make them comparable.

Source: OECD (2011), *Entrepreneurship at a Glance 2011*, OECD, Paris.

Intra-governmental co-ordination in policy development

The level of inter-ministerial co-ordination varies widely among EaP countries. Armenia and the Republic of Moldova both have a functional policy development body, a department within the Ministry of Economy (or equivalent), and a policy implementation agency. In Azerbaijan and Georgia, even though there is no institution responsible for SME policy development, a number of institutions, which maintain regular contact and co-operate with each other, deal with issues related to entrepreneurship and its regulatory framework.

The co-ordination of SME policy among various government stakeholders could be further enhanced in some EaP countries. In Azerbaijan currently elements of SME policy are covered by a range of ministries, but the impact could be improved through more

efficient communication and co-ordination. Furthermore in Azerbaijan and Belarus the Ministries of Economic Development and Economy, respectively, both develop and implement SME policy, infringing upon the transparency of the process and accountability of the institutions involved. In Ukraine, a new State Service on Regulatory Policy and Entrepreneurship was established but is not yet fully functional.

Box 5.2. **Intra-governmental co-ordination: The case of the UK**

In 2009, the United Kingdom merged the Department for Business, Enterprise and Regulatory Reform (BERR) and the Department for Innovation, Universities and Skills (BIUS) to form the Department for Business, Innovation and Skills (BIS). The new structure aims to build Britain's capabilities to compete in the global economy and to foster sustainable growth. The policy areas covered by the new department include: business regulations and law, consumer issues, enterprise and business support, trade and export control, higher education, innovation, science, statistics and other areas that affect directly or indirectly the competitiveness of firms. In order to create the best conditions for business growth, the department works in close co-operation with the private sector by conducting regular surveys and consultations with the business community. The BIS is further supported by a wide range of partner organisations, including nine executive agencies.

The Department is led by the departmental board which includes six ministers who form the strategic leadership of the department. The Board does not decide on policy, which continues to be determined by each minister. However, it gives advice and information on the operational implications of policies and the effectiveness of new policy proposals. The board meets bi-monthly and is chaired by the Secretary of State.

Source: Official website of the Department for Business, Innovation and Skills, *www.bis.gov.uk/*.

SME development strategy

Most EaP countries have short-term state programmes and action plans. Armenia, Belarus, the Republic of Moldova and Ukraine have state programmes for SME development which cover one to two years of specific measures. The programmes are generally only partially implemented due to a lack of funding. In addition the measures undertaken often do not follow any long-term goals and therefore lack coherence in time.

In Armenia, Belarus and the Republic of Moldova a long-term strategy is currently being developed. Its goal is to create a common vision of the expected long-term achievements in the area of SME development. The strategies pursue concrete measurable goals and are accompanied by action plans with specific measures to achieve those targets.

In Azerbaijan and Georgia, development of entrepreneurship is included in wider strategies for regional development or poverty reduction. This approach acknowledges the links with other policy areas and positions entrepreneurship development within the framework of national goals. Given that entrepreneurship is not the focus of any of these strategies, the documents do not define any measurable targets for SME sector development, which makes it difficult to assess the effectiveness of the implemented measures.

SME policy implementation agency or equivalent

To date, of the six EaP countries, only Armenia and the Republic of Moldova have a specialised agency which implements and co-ordinates the governmental programmes for SME development:

- In Armenia, the Small and Medium Entrepreneurship Development National Centre (SME DNC), established in 2002, implements the annual State programme for SME Support, with resources from the state budget. The agency is well staffed and financed. It employs 80 staff, with 50 of them operating outside Yerevan. From a budget of AMD 708.8 million (EUR 1.27 million), approximately 80% is provided by the state. Other resources are provided by various donors. SME DNC publishes annual reports on its activities.
- In the Republic of Moldova, the Organisation for Small and Medium Enterprise Development (ODIMM) is the main agency responsible for the SME policy State Programme for Sustaining the SME Sector Development. The agency is rather small (18 people) and is largely funded by donors.

Belarus and Georgia do not have a specialised agency for SME policy implementation. In Ukraine, a new state service has been established but is not yet functional, as the staff and the budget are not yet in place. With political support and adequate financing, the new service could play an important role in the policy-making process and become a leader in the area of small business support. In Azerbaijan, there are several executive agencies under the Ministry of Economic Development but communication and co-ordination could be further improved.

Box 5.3. **Institutional framework in the Republic of Moldova**

The development of SME policy in the Republic of Moldova is at a relatively early stage, but the building blocks for an institutionalised SME policy framework have been established. The SME policy is built around two main institutions: the Ministry of Economy, in charge of policy development, legislative drafting and policy co-ordination and the Organisation for the Development of the SME Sector of the Republic of Moldova (ODIMM) acting as an executive agency under the supervision of the Ministry of Economy. The legislative framework for SME policy is set by the Law No. 206-XVI/2007 which includes a comprehensive definition of SMEs, modelled on the EU definition, and provides guidelines for public policy in the area of SME development and support. In order to adopt a more consistent approach, an SME development strategy for the years 2012-20 was developed with the support of OECD. The strategy is expected to be adopted this year.

The task of SME policy implementation is assigned to ODIMM, founded in 2007, which acts as an executive agency under the supervision of the Ministry of Economy. ODIMM has a wide mandate which covers entrepreneurship promotion, service provision to SMEs and SME support in access to financing. It receives funds from the state budget for the implementation of state programmes but is otherwise self-financed. It is a public non-profit, non-commercial institution and implements a number of business support activities. ODIMM works in close co-operation with its development partners: the Ministry of Economy, the 33 regional councils, the Moldovan Investment and Export Promotion Organization (MIEPO), the Chamber of Commerce and Industry (CCI), the Agency for Innovation and Technology Transfer (AITT), regional development agencies, and business-related non-governmental organisations (NGOs) and associations.

Box 5.3. **Institutional framework in the Republic of Moldova** *(cont.)*

The *SME Development Strategy for 2012-2020*, developed with the support of OECD and with the involvement of all the relevant stakeholders, aims to ensure that the SME sector in the Republic of Moldova becomes a key factor leading to sustainable economic growth and increasing national competitiveness by creating a favourable entrepreneurial environment, promoting the entrepreneurial culture to support SMEs and to ensuring social cohesion. In order to achieve the vision and mission set out above, the government of the Republic of Moldova has identified six strategic objectives for the period 2012-20:

- Adapt the regulatory framework to the needs of SMEs.
- Improve SMEs' access to funding.
- Develop human capital by promoting entrepreneurial skills and culture.
- Increase competitiveness of SMEs and encourage the spirit of innovation.
- Facilitate regional development through SMEs.
- Develop business partnerships.

Each strategic priority incorporates specific objectives as specific foreseeable and quantifiable results, conducted through development plans, projects and actions included in the Action Plan for implementing the strategy, which will be developed every three years.

The Guillotine Working Group, which meets weekly, is the main platform for public-private consultation in the Republic of Moldova. It reviews all legislation that has an impact on business activities. Its primary function is to verify RIAs on draft legislation from the line ministries. Half of its 22 members are from the private sector, including a representative of the SME sector, and half are from the government. In developing the SME Strategy, the communication between the public sector, civil society, associations and other stakeholders has intensified and was an important element in the development of a feasible strategy accepted by all the parties.

Source: OECD (2011), *Republic of Moldova 2011: Fostering SME Development*, OECD, Paris, and follow-up actions.

Measures to tackle the informal economy

Operating in the informal sector is often a deliberate decision of individual firms and is based on the balance of costs and benefits of staying in or moving out of the formal sector. Creating conditions that would provide benefits to the firms operating formally, instead of penalising them, is an important step towards formalising the entire economy. It would also provide access to all the firms that need further state support. Although fiscal gains may be limited initially, formalisation is also associated with increased productivity, increased investment in human capital and more innovation. This could eventually lead to higher fiscal gains if the existing disincentives to formalise are removed.

In most EaP countries, the informal economy represents a large share of GDP. Its presence is usually the result of the low quality of public administration and institutions. Unfortunately there are no official statistical data across EaP countries for comparison.

Georgia is a specific case where the active fight against corruption and the informal economy started in 2004. The government has implemented a range of reforms to reduce corruption and the informal economy: reduction in the number of taxes, increase in the salaries of public servants and deregulation and simplification of administrative procedures.

Other countries do not have a separate strategy for tackling the informal economy. Armenia mentions reducing the informal economy as a goal in its wider national development strategy – the Sustainable Development Program of Armenia (2008). Even though this is not explicitly stated in a strategic document, some of the measures taken by Ukraine also aim to reduce informality, such as the recently adopted Tax Code that combines fiscal functions and stimulating mechanisms, the draft Pension Reform which aims to encourage reporting of real salaries and the Customs Code of Ukraine which is under review to decrease the number of licences and procedures for export/import. Important initiatives have also been undertaken by Azerbaijan which has adopted the National Strategy on Increasing Transparency and Combating Corruption and Action Plan 2007-11. The law on the Prevention of the Legalization of Criminally Obtained Funds or Other Property and the Financing of Terrorism was also adopted in February 2009. This resulted in the removal of the country from the Financial Action Task Force's "Black List". However, these measures mainly target corruption, not the informal economy.

Table 5.2. **Scores for sub-Dimension 3.1: Institutional framework**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
3.1.1.	SME Definition	5	2.5	3.5	3	5	4
3.1.2.	Availability of statistical data on SMEs	2	2	2.5	4.5	3	1.5
3.1.3.	Inter-governmental co-ordination in policy elaboration	3.5	3	3	3	3.5	2.5
3.1.4.	SME development strategy	2.5	2	1.5	2	2.5	1
3.1.5.	SME policy implementation agency or equivalent	4	2.5	1	1	3.5	2
3.1.6.	Measures to tackle the informal economy	3	1	1	4	2	1.5
Weighted average		***3.43***	***2.25***	***2.00***	***2.61***	***3.25***	***2.07***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Legislative simplification has been a priority for EaP countries, but systematic use of RIA could further support the development of a clear and transparent legal and regulatory environment

Managing the regulatory environment is an important aspect of the regulatory framework, allowing the government to keep policy making under control and not overburden the economic environment with laws and regulations. The development of a clear and transparent legal and regulatory environment is particularly important in the EaP region, as countries have had to eliminate obsolete pieces of legislation inherited from the former Soviet Union, as well as other regulations introduced during the process of transition.

Legislative simplification and elimination

Introducing legislation that is both simple and easy to understand for entrepreneurs is usually a very difficult task and government intervention should be structured around a well developed business environment simplification strategy. The strategy would ideally take the form of a multi-year policy agenda, explicitly aimed at continuously reducing legislative barriers, with clear identification of responsibilities, tasks, timelines for completion and evidence that targets have been implemented.

In recent years, reducing administrative barriers for SMEs has been a key priority for policy makers in the EaP region. Countries are at different stages in their implementation of strategies to simplify business-related legislation. In Georgia the review of legislation is ongoing, and over 12 000 legal acts were successfully eliminated from 2006 to 2010. The Republic of Moldova also undertook activities to review and simplify primary and secondary business-related legislation, from 2005 to 2008. Armenia, Belarus and Ukraine have all developed action plans or comprehensive strategies to simplify the business operating environment. However, the extent to which business simplification strategies call for legislative review and elimination of redundant laws and regulations is quite varied. In addition, countries do not explicitly identify the impact of legislation and regulations on SMEs as a key consideration in the legislative review process.

Regulatory impact analysis (RIA)

A formal introduction of RIA into the legislative system, calling for a comprehensive and obligatory analysis of all draft regulations, can be used to improve SME-related policy instruments and avoid introducing unnecessary legislation.

The legal framework for RIA is most advanced in the Republic of Moldova and Ukraine. In the Republic of Moldova, RIA is implemented by the Working Group of the State Commission for regulating entrepreneurial activity. In Ukraine, regulation was previously the responsibility of the State Committee of Ukraine for Regulatory Policy and Entrepreneurship (SCURPE). Following the dissolution of SCURPE in 2011, these responsibilities have been transferred to the Ministry of Economy. Armenia has also recently adopted a law for RIA, however evidence of its implementation is limited as the law only came into force in January 2011. On the other hand, Azerbaijan, Belarus and Georgia have not adopted a legal framework for RIA.

Apart from Armenia and the Republic of Moldova, EaP countries have not established a formal requirement to examine SME aspects during impact assessment, and further integration of the EU guidelines for the SME test within the legislation for RIA is needed. Specifically, countries should focus on including compulsory requirements for consultations with SME representatives, and a preliminary assessment and measurement of the potential impacts on SMEs. The creation of a comprehensive legal framework for the SME test should also be complemented by sound implementation mechanisms, and *ex post* analysis of the impact of new laws and regulations on SMEs.

Table 5.3. **Scores for sub-Dimension 3.2: Legislative simplification and regulatory impact analysis**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
3.2.1.	Review and simplification of current legislation	4	2	1.5	5	4	3
3.2.2.	Legislative guillotine	3	2	1.5	4.5	4.5	2.5
3.2.3.	Use of regulatory impact analysis (RIA)	2	1	1.5	2	4	2
3.2.4.	The SME test	1.5	1	1	1	3	1
Weighted average		***2.85***	***1.60***	***1.45***	***3.55***	***4.05***	***2.35***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Efficient and transparent public-private consultations needed to encourage the active participation of SMEs in the policy-making process

This section analyses the public-private consultation, which is one of the key tools for involving stakeholders in the policy-making process. Sub-Dimension 3.2 assesses the frequency, transparency, formal influence and inclusiveness of consultations between the public and private sectors in the EaP countries.

Armenia, Belarus, and Georgia have recently established new public-private consultation bodies to specifically discuss SME issues. However, these consultations are in their early stage and so far there has been only one meeting. Their effectiveness therefore cannot be properly assessed yet. The new bodies take the form of Councils (Committees) in Armenia, Belarus and the Republic of Moldova, and a Business Ombudsman in Georgia.

In Georgia, the Tax Ombudsman Office (a function introduced in 2011 within the framework of the new Tax Code) communicates with enterprises (both SMEs and large firms), aggregates their concerns and delivers them to the government in the form of suggestions and policy amendments. The consultations with the Tax Ombudsman (as well as with the Revenue Service) are held permanently including online.

The Entrepreneurship Council under the President of the Republic of Azerbaijan was created in 2002. Its main purpose is to promote the development of entrepreneurship and to prepare suggestions for the President of the Republic of Azerbaijan. In Ukraine the same role is performed by the regional councils of entrepreneurs. However, the frequency of these meetings is sporadic.

In most of the EaP countries public hearings are also widely used to discuss draft legal acts. Public hearings, compulsory in all countries except Azerbaijan, are open meetings where interested stakeholders can voice their opinion or concerns about a draft legal act. Posting the draft legal acts online for comment is also a popular way of involving stakeholders in the process. The formal influence and effectiveness of these types of consultations are usually limited, because the process is based on reactive one-way communication (from the private sector to the government). In both cases the government is not obliged to respond and it may or may not consider the comments for the final amendment of the act.

Table 5.4. **Scores for sub-Dimension 3.3: Public-private dialogue**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
3.3.1	Frequency and transparency of public/private consultations (PPCs)	3	2	2	4.5	3.5	2
3.3.2	Formal influence of PPCs	2	1.5	2	4	3	2
3.3.3	Representativity of PPCs	2.5	2	2.5	3	3	2
Weighted average		***2.50***	***1.83***	***2.17***	***3.83***	***3.17***	***2.00***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

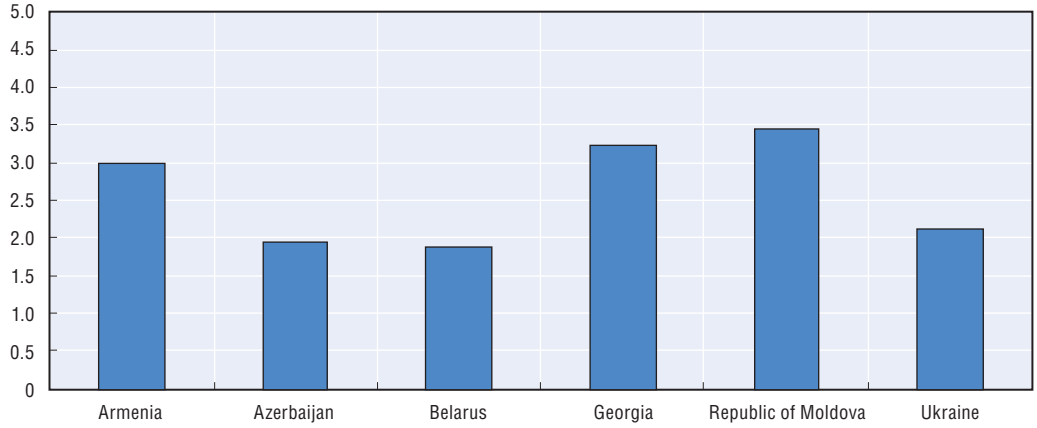
For all the EaP countries the focus should be on developing transparent and inclusive organisations that facilitate public-private dialogue, such as professional associations, business associations, employers' confederations and chambers of commerce. These organisations should be encouraged but not controlled by the government to ensure their

transparency and the representativity of the dialogue between the government and the private sector. Moreover, effectiveness of the dialogue could be further improved by streamlining the organisational process based on EU and OECD guidelines for effective public-private consultations, such as ensuring that the schedules and documentation are available in advance, as well as timely notification about upcoming meetings.

All the countries should focus on developing a strong long-term SME strategy that would build a common vision on how the private sector should develop (not necessarily only SMEs), and which could give weight to supporting small enterprises. The focus should be on further ensuring its implementation via intra-governmental co-ordination and a properly financed action plan tailored to its strategic goals. The countries should also make sure that both the strategy and the programmes are monitored and evaluated.

Statistical data on the small business sector could be further improved. A lack of accurate, detailed and up-to-date information hinders the ability of policy makers to accurately assess the situation in the SME sectors in order to develop appropriate policies. Moreover, to ensure international comparability, the definition of SMEs can be synchronised or approximated to the EU definition. Joining the OECD-Eurostat EIP would provide a constant and accurate flow of information about SMEs. This could provide comparison both within the region and with other countries.

Figure 5.2. **Weighted scores for Dimension 3: Regulatory framework for SME policy making**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 6

Operational Environment for SMEs (Dimension 4)

Make public administrations responsive to SMEs' needs
(Small Business Act Principle 4)

Dimension 4 of the Small Business Act (SBA) assesses the extent to which public administrations have developed instruments to simplify regulations and reduce costs and procedures for SMEs. It has two sub-dimensions: the company registration process, and interaction with online government services (e-government).

In recent years, Eastern Partner (EaP) countries have made significant progress in reforming the operational environment for SMEs. In particular, reforms to the company registration process have led to the removal of overly burdensome regulations, saving time and reducing costs for SMEs and entrepreneurs. In some cases, countries have redesigned the registration process by overhauling inefficient institutions and bringing administrative procedures in line with world standards. The introduction of e-government services in the EaP region has also led to a reduced administrative burden and greater accessibility to public services for SMEs. Countries are developing a range of e-government services, from electronic signatures to increasing connectivity between public administration databases.

Introduction

Before entering the business environment, entrepreneurs are typically required to register with the public administration. The cost and complexity of the company registration process can discourage entrepreneurial activity and act as a significant barrier for new start-ups. The impact of lengthy and costly company registration procedures is felt most heavily by micro and small-sized enterprises, as they divert human and financial resources away from business activity just when the company is most fragile.

Box 6.1. **Company registration reforms in OECD countries**

In recent years, efforts by OECD countries to streamline procedures and reduce costs in dealing with the public administration have led to substantial improvements in the efficiency of the company registration process. According to the World Bank's *Doing Business 2012* report, the average time to register a firm in high income OECD countries fell from 22 days in 2006 to 12 days in 2012. The average cost of registration also fell considerably, from 8.2% to 4.7% of income per capita (World Bank, 2012). These improvements are largely the result of the application of new and innovative information and communications technology (ICT) solutions such as electronic company registers, one-stop-shops for company registration, and online registration facilities.

Source: World Bank (2012), *Doing Business 2012*.

Efforts to simplify the operational environment and reduce the administrative burden on SMEs can also extend beyond reforms to the company registration process. SMEs need to interact with the public administration throughout their life cycle, to obtain permits and licenses, file taxes, and participate in public procurement. Today, governments are increasingly turning to technology to deliver innovative reforms to public services. The development of e-government allows for a variety of services to be delivered online, resulting in lower costs for entrepreneurs and the public administration, less red tape and reduced informal activities.

Assessment framework

The assessment framework for Dimension 4 is modelled on the approach adopted by the European Commission and includes two main sections. The first section analyses in detail the process of company registration, which can be divided into three phases:

i) The first phase covers issuing of the company registration certificate. In most cases, the registration act is issued by a court or specialised company registration agency.

ii) The second phase covers notification of the establishment of a new company to various branches of the central and local public administration that deal with the private sector (*e.g.* tax administration, employment and labour agencies, customs administration and office of statistics).

iii) The third phase covers all the procedures necessary to ensure compliance with the country's legislative and regulatory framework. When these procedures are completed, licences and permits are issued.

This sub-dimension is composed of ten indicators, organised into four sections: issuing of the company registration certificate, registration notification, completion of the overall registration process and advanced registration procedures.

Figure 6.1. **Assessment framework for Dimension 4: Operational environment for SMEs**

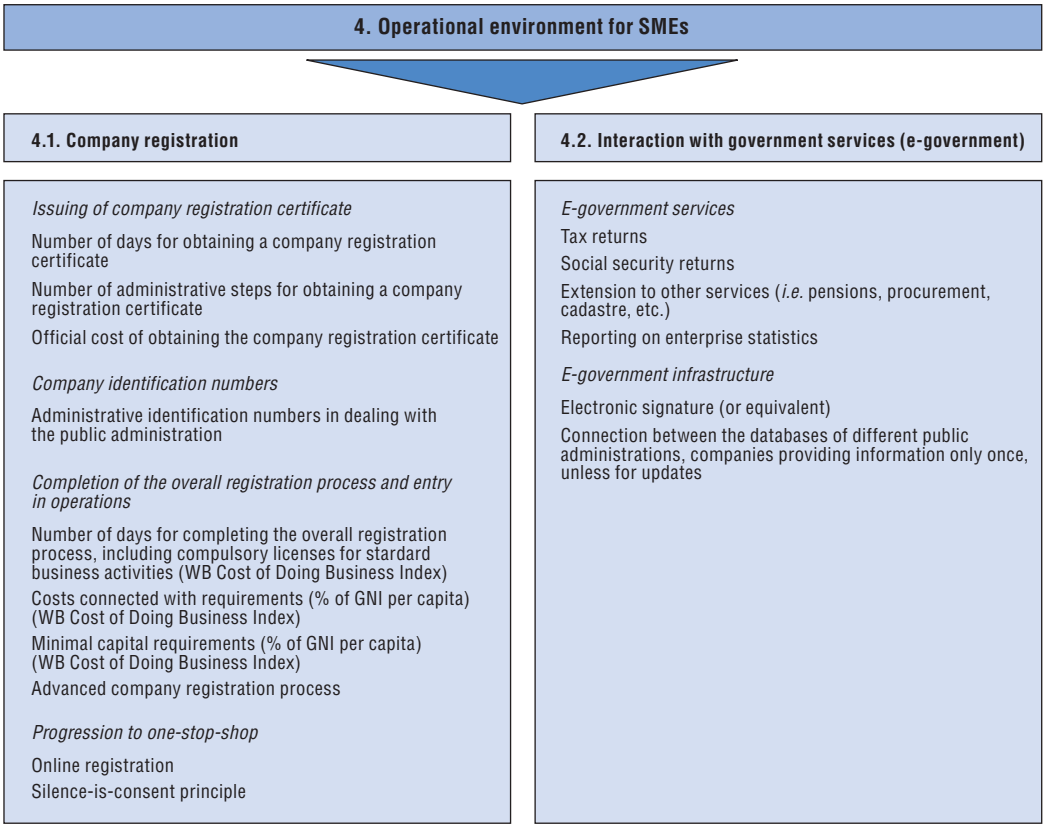
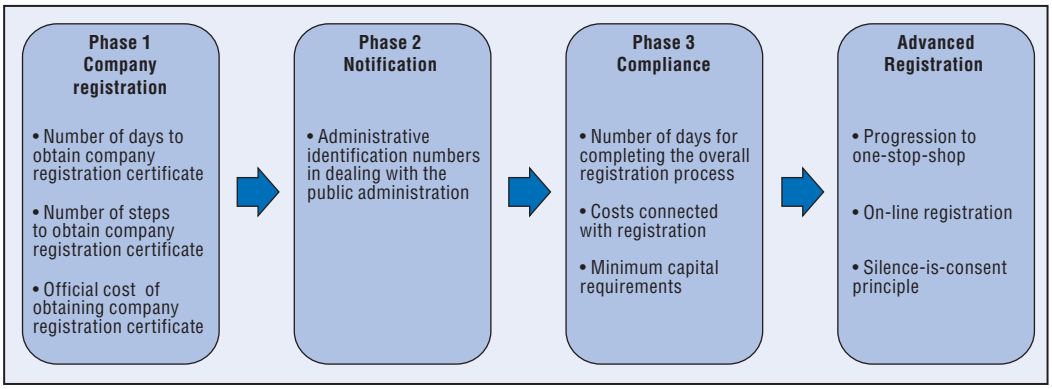


Figure 6.2. **The three phases of company registration**



The second sub-dimension focuses on online interaction with government services, and is composed of six indicators structured into two sections: e-government services and e-government infrastructure.

This sub-dimension measures the development of online support services that encourage increased interaction between SMEs and the public administration. Online access to government services is of particular importance to the small businesses sector, as entrepreneurs are typically unable to spend extensive time and resources interacting directly with the public administration. Within the EU, there has been an increasing trend towards the adoption of sophisticated online support services (*e.g.* online filing of tax returns, social security returns, reporting on enterprise statistics, etc.). By adopting information and communication technology (ICT) solutions, governments can reduce costs for SMEs and simultaneously improve the quality and efficiency of their services. ICT solutions also play an important role in reducing corruption and informal sector activities by improving enforcement mechanisms, increasing transparency and reducing subjective decision making by government officials (ADB, 2001).

Promoting the development of e-government services and ICT solutions is a cornerstone of the EU flagship initiative "A Digital Agenda for Europe" and the "Europe 2020" growth strategy. As small businesses adopt ICT solutions, they will be able to establish electronic links with businesses and government support services and access new sources of information to enhance innovation and competitiveness (European Commission, 2010).

Analysis

EaP countries have achieved significant progress in the area of company registration, saving time, reducing costs and removing administrative barriers for SMEs

Phase 1: Company registration

Reforms to the company registration process typically involve simple and targeted measures to restructure and improve the efficiency of the existing registration body. This may involve reducing the cost or time needed for entrepreneurs to obtain a company registration certificate, leaving registration procedures largely unchanged. Alternatively, governments may decide to introduce more extensive reforms by creating a new company register, establishing one-stop-shops and streamlining procedures for company registration.

Table 6.1. **Phase 1: Issuing of company registration certificate**

	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
Number of days to obtain company registration certificate	5 days	6 days	3 days	1 day	5 days[1]	8 days
Number of administrative steps to obtain company registration certificate	3 steps	4 steps	3 steps	1 step	3 steps	4 steps
Official cost of obtaining company registration certificate	Approx. EUR 33	Approx. EUR 10	Approx. EUR 22	Approx. EUR 42	Approx. EUR 45	Approx. EUR 15

1. One day for an additional fee.
Source: World Bank (2012), *Doing Business 2012*.

In recent years, EaP countries have introduced significant reforms to the company registration process, removing overly burdensome regulations that discourage the creation of new enterprises. In a number of cases, countries have completely redesigned the

registration process, by overhauling inefficient institutions and bringing administrative procedures in line with the world's most competitive standards.

EaP countries can be divided into two groups according to their progress in the implementation of reforms to the company registration process. The first group consists of Armenia, Azerbaijan, Belarus and Georgia. In these countries, one-stop-shops have been established as the first point of contact for entrepreneurs. Registration offices also provide a number of other services in addition to company registration, such as registration with the tax office and statistical authorities.

The second group includes the Republic of Moldova and Ukraine. Countries in this group have also introduced substantial reforms to company registration, including the reduction of legal time limits for issuing company registration certificates and the establishment of one-stop-shops for the registration of companies and individual entrepreneurs. However, entrepreneurs are still required to undertake a number of procedures before filing their documents with the company registrar. In Ukraine, for instance, entrepreneurs are required to notarise the company charter and execute premises, open a bank account for initial capital and pay the registration fee at a bank before registering at the Registration Office.

Phase 2: Notification

The notification process is a central part of the company registration process, as it involves direct communication of the newly established entity to key areas of the public administration. Reforms to this phase have typically focused on transferring the burden of notification away from the company, by increasing communication between the company register and government agencies that interact with the private sector (*e.g.* tax office, employment and labour agencies, customs administration, office of statistics)

Table 6.2. **Phase 2: The notification process**

	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
Administrative identification numbers in dealing with the public administration	2 numbers	1 number	3 numbers	1 number	2 numbers	1 number

Source: World Bank (2012), *Doing Business 2012*.

EaP countries have made considerable progress in reducing the number of company identification numbers issued during the registration process. However, after obtaining the company registration certificate, entrepreneurs are still obliged to register with a number of additional government offices and agencies. For instance, in the Republic of Moldova, just two administrative identification numbers are issued during the registration process: a state identification number (IDNO) and a statistical code for use by the National Bureau of Statistics. However, communication is not well established amongst government institutions, and as a result start-ups are still required to register with the following administrative authorities: State Registration Chamber (1-5 days); Ministry of Information Technologies and Communication (1 day, included in the registration process); Territorial State Fiscal Inspectorate (1-3 days); Social Security Fund (1 day); and National Medical Insurance Company (2 days). Entrepreneurs in Ukraine are faced with similar requirements. Despite having just one ID code generated by the National State Registry of

Ukrainian Enterprises and Oganizations (EDRPOU), entrepreneurs are required to spend additional time and undergo additional costs in registering with the State Statistics Committee (1 day), registering VAT at the State Tax Authority (10 days), and notifying the District Tax Inspectorate of the opening of a permanent bank account (2 days).

Only Georgia is able to issue a single identification number during the registration process without requiring entrepreneurs to register with additional authorities. To build on the considerable progress already achieved in this area, EaP countries should focus on establishing functional electronic company registers, and one-stop-shops that allow for all necessary registration and notification procedures to be completed in the same location. These reforms would allow for the collection of reliable business statistics, improve the flow of information between government agencies and institutions, and typically lead to the issuing of fewer company identification numbers by the public administration. Electronic company registers also allow for efficient dissemination of business information and create opportunities for integration with European business information networks.

Phase 3: Compliance

From an entrepreneur's perspective, the overall registration process must be fast, efficient and cost-effective, facilitating smooth entry of the company into the business operating environment. Substantial reforms to company registration should address the entire process, including the compliance phase. However, reforms to the compliance phase affect the operation of several government agencies and may require the review of numerous laws, regulations and procedures.

Discrepancies between the number of days and the cost of issuing the company registration certificate (Indicators 4.1.1 and 4.1.2) and the number of days and cost of completing the overall registration process (Indicators 4.1.5 and 4.1.6) reflect the impact of public and private players such as notaries, lawyers, municipal authorities and government agencies other than those directly involved in Phases 1 and 2. In particular, the need to obtain licences and permits from the central or local administration can be a significant constraint for new start-ups.

Table 6.3. **Phase 3: Compliance**

	Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
Number of days for completing the overall registration process, including compulsory licences for standard business activities	8 days	8 days	5 days	2 days	9 days	24 days
Costs connected with registration (% of GNI per capita)	2.9	2.7	1.3	4.3	9.1	4.4
Minimum capital requirements (% of GNI per capita)	0	0	0	0	9.9	1.8

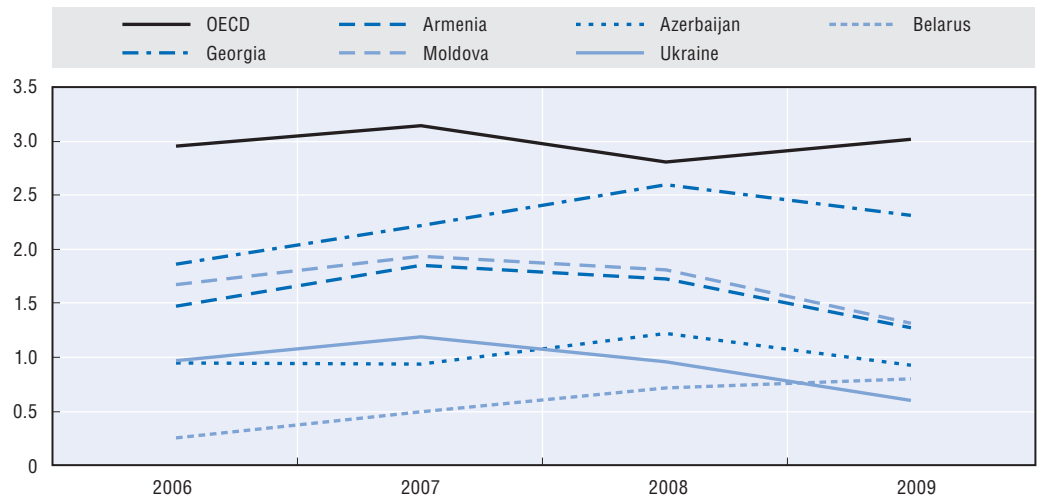
Source: World Bank (2012), *Doing Business 2012*.

The data for Indicators 4.1.5, 4.1.6 and 4.1.7 was taken from the 2012 World Bank *Doing Business* report. However, it is important to note that the *Doing Business* indicators are only relevant for the registration of limited liability companies, and do not take into consideration simplified procedures for individual entrepreneurs. In Georgia and the Republic of Moldova, the official cost of registration is substantially lower for individual entrepreneurs.

Although EaP countries have made significant progress in reforming the company registration process, efforts to introduce a more streamlined system have not always filtered down to the level of the local government administration where companies are actually dealt with. In Ukraine for instance, it takes an average of 24 days to establish a company, 8 of which are spent completing the 4 steps needed to obtain a company registration certificate. The minimum capital requirement also presents additional costs for new start-ups. Minimum capital requirements for limited liability companies have been abolished in Armenia, Azerbaijan, Belarus and Georgia. In the Republic of Moldova, however, the total cost of registration is 9.1% of GNI per capita. This represents a considerably higher proportion than in other EaP countries and may act as a significant barrier for entrepreneurs.

The impact of these overly burdensome regulations is reflected in raw measures of entrepreneurship such as new business density (new registrations per 1 000 people aged 15-64). As shown in Figure 6.3, new business density is particularly low in EaP countries, when compared to the OECD average. Countries should now devote their attention to shortening the notification phase, removing unnecessary requirements to obtain permits and licenses, and further reducing the time and cost to complete the overall registration process.

Figure 6.3. **New business density (new registrations per 1 000 people aged 15-64**



Source: World Bank/*World Development Indicators*.

Advanced company registration process

One-stop-shops for company registration are available in all EaP countries. However, the effectiveness of one-stop-shops is highly variable across the region, and depends largely on the one-stop-shop's capacity to integrate all necessary registration, notification and compliance procedures within the same institution. Following the submission of all necessary documentation, entrepreneurs in Armenia, Azerbaijan, Belarus and Georgia are not required to undertake many additional procedures to complete the registration process. In Armenia, for instance, new start-ups are only required to pay the registration fees at a bank and order a company seal (not officially required by law). In the Republic of Moldova and Ukraine, one-stop-shops do not effectively reduce the administrative burden on entrepreneurs. In Ukraine, for instance, an additional 16 days and 5 administrative procedures are needed to register with various government authorities and complete all necessary notification and compliance procedures.

For many EaP countries, online registration is still in its early stages. Only Armenia has developed a fully functional online registration system, allowing for most stages of the company registration process to be completed via the Internet. However, the website does not have a solid track record, as it was only launched in March 2011. Furthermore, limited adoption of the Internet by SMEs in regional areas of Armenia restricts the potential demand for online registration services. According to the *World Development Indicators Database*, Armenia has the lowest rate of Internet usage in the EaP region (see Figure 6.4). Other EaP countries should take advantage of recent growth in Internet use rates, and develop functional online registration systems for entrepreneurs.

The silence-is-consent principle is an effective way of transferring the costs associated with administrative delays from the entrepreneur to the government. When applied to company registration and general business licences, it can often speed up and improve the company establishment process. By setting a clear timeframe for completing the registration and licensing process, the business owner can effectively plan the start of business operations. However, the silence-is-consent principle cannot be applied to cases where the risks associated with non-compliance by the applicant are high. For instance, the issuing of business licences that require meeting specific health and environmental standards may require strict controls for the monitoring and screening of applications. Governments can speed up these procedures by setting a deadline for the completion of all necessary tasks, and by regularly monitoring the performance of relevant government agencies and institutions.

Some provisions for the silence-is-consent principle may be found in the legislation of Armenia, Georgia, the Republic of Moldova and Ukraine. In most cases, the principle has only recently been introduced for the company registration process and general business licences. The silence-is-consent principle is not included in the legislation of Azerbaijan and Belarus. Only the Republic of Moldova has a general clause in the Law on the Regulation of

Table 6.4. **Scores for sub-Dimension 4.1: Company registration**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
4.1.1.	Number of days for obtaining a company registration certificate	4	3	4	5	4	3
4.1.2.	Number of administrative steps for obtaining a company registration certificate	4	4	4	5	4	4
4.1.3.	Official cost of obtaining the company registration certificate	4	5	4	3	4	4
4.1.4.	Administrative identification numbers in dealing with the public administration	4	5	4	5	4	5
4.1.5.	Number of days for completing the overall registration process, including compulsory licenses for standard business activities (WB, *Cost of Doing Business Index*)	3	3	4	4	3	2
4.1.6.	Costs connected with registration (% of GNI per capita) – (WB, *Cost of Doing Business Index*)	3	3	4	3	2	3
4.1.7.	Minimal capital requirements (% of GNI per capita) – (WB, *Cost of Doing Business Index*)	5	5	5	5	4	4
4.1.8.	Progression to one-stop-shop (OSS)	4	4	5	5	4	4
4.1.9.	Online registration	4	3.5	2.5	2	2	1.5
4.1.10.	Silence-is-consent principle	2	2	1	5	3	3
Weighted scores		***3.89***	***4.16***	***3.98***	***4.20***	***3.63***	***3.74***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Entrepreneurial Activity of 20 July 2006 for the adoption of the principle by all government institutions involved in regulatory activities. To encourage further implementation of the concept in other key areas of the administration, EaP countries could introduce the silence-is-consent principle under a separate legislative act. This will establish the foundations for adoption of the silence-is-consent principle as a standard administrative practice.

The introduction of e-government services in EaP countries can reduce administrative costs for SMEs, improve the quality and efficiency of government services and reduce corruption and informal sector activities

Online filing of tax returns and social security returns

The ability of companies to file tax returns and social security returns online is essential, particularly if governments wish to reduce collection costs, simplify existing procedures and devote more resources to the provision of information and support services for taxpayers. Online filing also leads to reduced costs for firms in complying with government tax requirements, and increased ability to estimate tax liabilities.

All countries in the EaP region have introduced a legal framework to allow for online filing of tax returns. However, progress in the implementation of new systems is more varied. Georgia has established the most sophisticated online tax filing system in the region, with software that allows for online credit and debit compensation. Taxpayers in Georgia can pay corporate income tax, property tax, and value added tax (VAT) online. Armenia, Azerbaijan and Belarus allow for online filing of corporate income tax and VAT, but some restrictions remain before all tax-related activities will be available online. In the Republic of Moldova and Ukraine, technical issues pertaining to the software and the accreditation of electronic signatures are preventing widespread and effective usage of online tax filing systems.

Less progress has been made in facilitating online filing of social security returns. At present, social security returns can only be filed online in Armenia and Belarus. It is interesting to note that as a result of reforms to simplify the Georgian Tax Code, social security contributions were reduced from 31% to 20% in 2005 and were entirely abolished in January 2008. Consequently, there are no compulsory requirements for firms in Georgia to pay social security contributions from employee wages.

Box 6.2. **E-government in Azerbaijan**

Electronic filing of tax returns has been available in Azerbaijan since 2006 through the Ministry of Taxes. Online submission of tax returns and online exchanges of tax-related information has led to reduced administrative costs for both the government and the private sector. The government is currently working to increase the range of online services available to entrepreneurs under the action plan of the "State Program on Development of Communications and Information Technologies in the Republic of Azerbaijan in 2010-12 (E-Azerbaijan)". The Ministry of Communication and Information Technology is also in the process of establishing a specialised state agency in charge of e-government, and additional online services such as an online cadastre registry are expected to be introduced by the end of 2012.

Azerbaijan has taken positive steps to further developing their infrastructure for e-government. In particular, the recent introduction of an electronic signature system and the establishment of an operational accreditation body (National Certification Services Centre) has contributed towards enabling direct interaction between SMEs and the government.

Extension to other services (i.e. pensions, procurement, cadastre)

A clear and comprehensive strategy for e-government is a precondition for the development of a wide range of online services. Georgia is the most advanced in the region, and has developed a range of functioning e-government services including online cadastre, procurement and customs declarations. In 2005 the Republic of Moldova adopted "Electronic Moldova", a national strategy for the development of an ICT-based society. However, so far its implementation has not been successful. Armenia has also recently approved a plan to further develop online services (*e.g.* online pensions and procurement), and has designed an online e-government portal in an effort to encourage SMEs to adopt electronic forms of communication.

Pilot projects and *ad hoc* initiatives have been established in Armenia, Belarus and Ukraine to allow for online filing of pensions. To encourage greater online interaction between SMEs and the public administration, countries (in particular Azerbaijan, Belarus and Ukraine) would benefit from a strategic approach to the development of a broad range of e-government services. In addition, maintenance costs of online services can be quite high. Thus it is important to establish realistic budgets for the creation of sustainable e-government services, and ensure that implementation is carried out in a timely manner.

Reporting on enterprise statistics

Online reporting on enterprise statistics is in its infancy in the EaP region. At present only Ukraine allows enterprises to submit statistical reports online. However there is a need to increase the sophistication of current software and encourage more widespread use by SMEs. The National Statistics Office of Georgia posts statistical surveys online; however these have to be submitted by e-mail or by post, due to the lack of a functioning online reporting system. Although strategies have been approved in Armenia and Republic of Moldova, online reporting of enterprise statistics is currently not available in Armenia, Azerbaijan, Belarus or the Republic of Moldova.

Electronic signature (or equivalent)

Electronic signatures enable direct communication between SMEs and the public administration, and allow for legally enforceable procedures to be conducted online. A functioning electronic signature system with a legitimate and operational accreditation body is a precondition for the development of advanced and sophisticated e-government services.

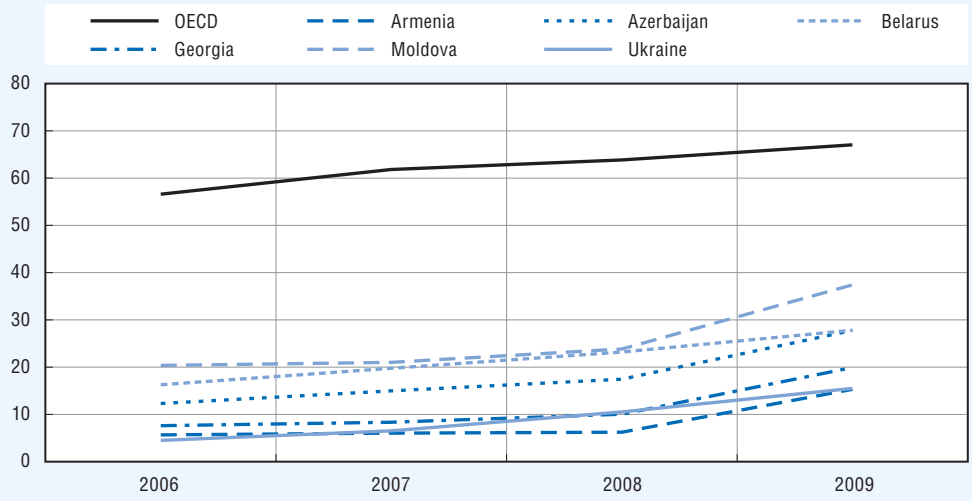
All EaP countries have adopted a legal framework for electronic signature and the approval of electronic documents. However, the implementation of electronic signature is more limited, and is typically only available for online filing of tax returns. In Georgia, SMEs are able to use alternate means to validate electronic documents. For instance, the Revenue Service of the Ministry of Finance assigns a unique username and password to each taxpayer, allowing for effective online filing of tax returns. Further implementation of electronic signature should be encouraged for other forms of e-government. In addition, there is a strong need for countries to ensure that functional and legitimate accreditation bodies are in place to provide certification services for electronic signatures.

Box 6.3. **Online access in the EaP region**

High quality digital infrastructure is needed for SMEs to adopt electronic forms of communication and to create linkages between SMEs and government support services. In the EaP region, Internet access is restricted due to high infrastructure costs, particularly in non-central areas. Limited adoption of the Internet by SMEs restricts the potential demand for e-government and online support services.

Online access in the EaP region has improved substantially in recent years. Countries should take advantage of recent growth in Internet usage rates by developing state-of-the-art online support services for SMEs.

Figure 6.4. **Internet users (per 100 people) in the EaP countries**



Source: World Bank/*World Development Indicators*.

Connection between the databases of public administrations

The provision of a favourable administrative environment for SMEs requires significant co-ordination amongst government ministries and public institutions. Increased database connectivity allows public institutions to provide high quality services to small business owners, and reduces the likelihood of SMEs being asked to provide the same information to different offices of the public administration.

All governments in the region have taken steps towards improving connections between the databases of public administrations, but the extent to which this has been effective in reducing the administrative burden on SMEs varies. In many cases, countries have used reforms to the company registration process as a starting point. For instance, Belarus has developed an automated system of data exchange between the Unified State Register and various public authorities involved in the registration process. Georgia has the most advanced system of data exchange in the region. Information is automatically exchanged between key offices of the public administration, including the National Agency of Public Registry, tax administration office, cadastral data, national archives and enforcement services.

In Armenia, the Republic of Moldova and Ukraine administrative blocks are preventing new electronic data-sharing systems from being used to their full capacity. A number of ministries and public institutions in Armenia have adopted Mulberry Groupware, a specialised workflow management system that facilitates centralised storage of electronic documents. The Republic of Moldova and Ukraine have also taken steps to make their company registers accessible to other offices of the public administration. In addition to updating current systems to reflect the latest advances in technology, increased co-ordination between government bodies is needed to ensure that new electronic data sharing systems are effective in reducing the administrative burden on SMEs.

Table 6.5. **Scores for sub-Dimension 4.2: Interaction with government services (e-government)**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
4.2.1.	Tax returns	4	4	4	5	4	4
4.2.2.	Social security returns	4	2	4	5	2	3
4.2.3.	Extension to other services (*i.e.* pensions, procurement, cadastre, etc.)	2	2.5	2	4	3	2
4.2.4.	Reporting on enterprise statistics	2	1	1	3	3	4
4.2.5.	Electronic signature (or equivalent)	4	4	4	4	3	3
4.2.6.	Connection between the databases of different public administrations, companies providing information only once, unless for updates	2	3	3	5	2	2
Weighted scores		***3.33***	***3.13***	***3.42***	***4.42***	***2.83***	***3.00***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

The scores for this dimension show that EaP countries have made significant progress in reforming the company registration process, both in terms of time and cost reduction. In most cases, the overall time and cost required to set up a business is lower than the OECD average. The introduction of e-government services in EaP countries has also led to reduced administrative costs and greater accessibility to government services for SMEs.

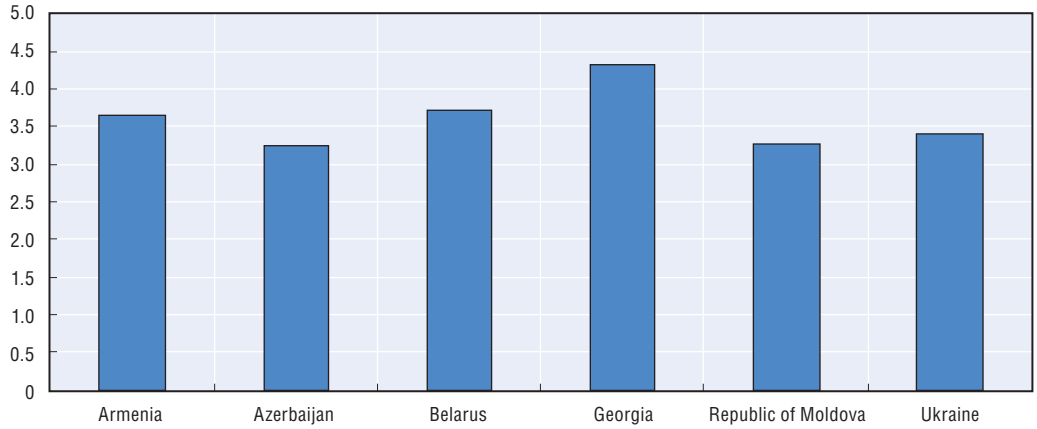
Although EaP countries have made significant progress in reforming the company registration process, efforts to introduce a more streamlined system have not always filtered down to the level of the local government administration where companies are actually dealt with. In particular, progress is still hampered by the pre- and post-registration compliance procedures that must be completed before companies can begin operating. To further build on the considerable progress already achieved in this area, countries should now turn their attention to introducing online registration systems, electronic company registers and addressing factors that delay the completion of the start-up process.

Further reforms should also focus on increasing the capacity of one-stop-shops to complete all necessary registration and notification procedures at one window. Following the example of Georgia, EaP countries should facilitate co-ordination between various branches of the central and local administration involved in the registration process.

Countries should also take advantage of new ICT solutions to introduce functional e-government services and online registration facilities. Online services are of particular

importance, as they allow governments to reduce costs for SMEs, improve the quality and efficiency of their services, and reduce corruption and informal sector activities. In the EaP region, there is a need to introduce new systems or upgrade existing services, allowing SMEs to perform sophisticated functions online and increase their level of interaction with the public administration.

Figure 6.5. **Weighted scores for Dimension 4: Operational environment for SMEs**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 7

Support services for SMEs and start-ups and public procurement (Dimensions 5a and 5b)

Adapt public policy tools to SME needs (SBA Principle 5)

SMEs face many barriers that prevent their start-up or growth and hamper their potential. They have less access to markets and procurement because of a lack of information on existing opportunities or discouraging, complicated procedures. This chapter analyses the limited access of SMEs to markets and procurement and the role of government in identifying these market failures and applying policy tools to address them. It is divided into two policy dimensions: Business services and public procurement. The first policy dimension gives an overview of the public policy tools to address information gaps, financial support for start-ups and the limited availability of business services for small firms. The second focuses on giving SMEs an equal chance to participate in public procurement by publishing procurement, opening bidding to foreign companies and introducing E-procurement.

DIMENSION 5A: SUPPORT SERVICES FOR SMES AND START-UPS

Introduction

The market for business services has many gaps and failures that disproportionately affect SMEs.[1] The less developed the economy and the market for business services, the more intense are the market failures that affect SMEs. Providing business support to SMEs can partially alleviate this imbalance and boost the competitiveness of SMEs.

The type of support needed by the SME sector depends on the specific type of activity of the firm and its stage of development. SMEs generally require, and could benefit from, support in the following areas: information, customer focus advice and support (consulting), skills and management development (through training of existing staff or recruitment of additional staff), financial support and infrastructure (including work space). These areas impose significant costs on a small, single firm, especially in the context of limited financing. Compared to large firms, which can generate a large amount of information internally, can organise trainings for the staff and have much lower fixed costs of infrastructure, small firms prefer to avoid investing in these services. They have limited knowledge about the effectiveness and potential impact of these services on their competitiveness and have limited available funds.

From the supply point of view, the lack of business services for SMEs is largely due to the high transaction costs involved in offering these services. Within the SME sector, economic activities are much more diverse and heterogeneous from firm to firm, compared to large enterprises where the process is more standardised. As a result, advisory or other business services must be tailored to each separate case. This imposes higher costs on the service provider.

This sub-chapter measures the extent to which the government supports small businesses by providing business information and other business support services for SMEs and start-ups.

Box 7.1. **SMEs, the local environment and the importance of public-private partnerships: Trentino-Svillupo Case**

An important feature of SMEs is that their development is very complex. Unlike large firms, both the internal features of the firm and the local context determine the final outcome (success or failure) of the business initiative. The effect goes both ways – from firm to local environment and from the local environment to firm:

- On the one hand, the level of development of the environment and the specific features of the region (*e.g.* specialisation, demographic characteristics, etc. may determine the outcome of the business. Moreover, SMEs interact on a permanent basis with local governments rather than with national institutions, and therefore are directly affected by their quality and effectiveness.

Box 7.1. **SMEs, the local environment and the importance of public-private partnerships: Trentino-Svillupo Case** *(cont.)*

- On the other hand, the development of business increases the likelihood that the region will develop even further, will foster the development of new businesses and growth of existing ones and will increase the demand for other products and services by employing people and paying salaries.

In this way, apart from the financial returns generated by the firm to its owner, SMEs provide important social returns for the region. Although these returns are usually not accounted for at the level of an individual firm, regional/local governments should not overlook this important role of SMEs.

Trentino Sviluppo is the agency set up by the Autonomous Province of Trento, Italy to foster the sustainable development of the Trentino system by taking action and providing services aimed at supporting the growth of business skills and nurturing the capacity for innovation. The agency is specialised in scientific and technological parks, real estate, equity investment and infrastructure, entrepreneurial and territorial development, the creation of clusters, and many other types of support.

The agency provides a wide range of services to firms in their pre-seed, seed and start-up stages, including:

- Providing assistance to self-employed businessmen, which includes information evenings, individual interviews, training meetings and meetings to analyse and check the job plan.
- Pre-incubation facilities, with dedicated areas and orientation assistance to help entrepreneurs devise their marketing plan or their legal, economic and financial profile.
- Incubation facilities: six business innovation centres for companies at the start-up stage and research centres with production areas, services and fully equipped laboratories.
- A fund with seed money designed to promote the spread of business initiatives in innovative or high-tech areas, that can be used to cover part of the start-up costs.
- Free-of-charge training and information sessions intended for small and medium-sized enterprises, and run on a concrete operational basis, both in terms of the topics chosen for discussion and in terms of how they are managed, as well as more structured courses and training sessions

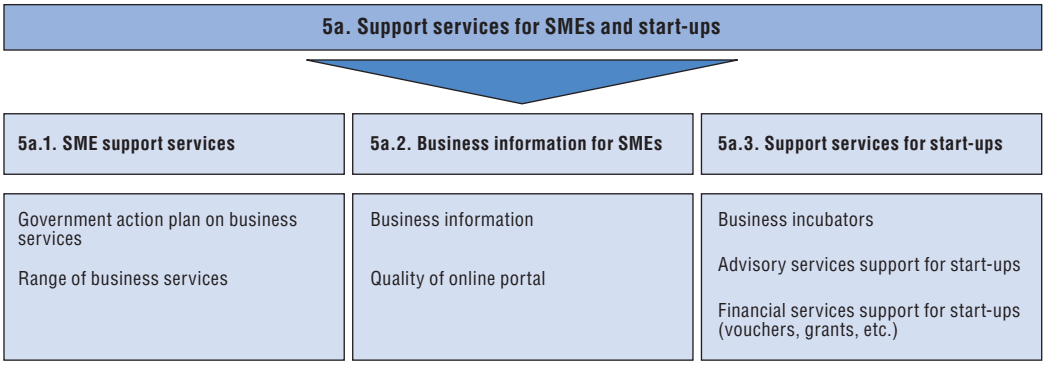
Sources: Trento presentation; Vinnell and Hamilton (1999); "Trentino Sviluppo: the SME Service Value Chain in Trentino", by Luca Capra, Director, Entrepreneurship and Development Area, Trentino Sviluppo.

Assessment framework

The dimension on support services and start-ups has three sub-dimensions (Figure 7.1).

The first sub-Dimension 5a.1 assesses the existence and efficiency of a systemic approach to tackle the market failures that affect SMEs as well as the range and outreach of the market for business services. The sub-dimension has two indicators that assess the range and outreach of the market of business services and the existence and implementation of a systemic approach for detecting and tackling market failures. A systemic approach facilitates the identification of problems that persist in the market for different groups of SMEs, and allows for greater co-ordination between different initiatives to avoid unnecessary overlaps. Eventually it facilitates a more efficient use of public resources by targeting the most common and prevailing problems and choosing the most effective tools to address them.

Figure 7.1. **Assessment framework for Dimension 5a: Support services for SMEs and start-ups**



The second sub-Dimension 5a.2 measures the availability of information on doing business for firms through business centres or the Internet. The availability of information about services, advisory support and support for doing business (registration, export/import procedures and other basic operations), is an important step towards better informed and thus better managed enterprises. A properly communicated support scheme or programme will also reach a larger proportion of SMEs and is more likely to attract the firms that are in most need of such support. Different channels of communication as well as easily accessible and nationally recognised information centres or online portals are therefore crucial for both SMEs and policy makers.

Finally, sub-Dimension 5a.3 looks at the measures undertaken by the government to support start-ups, such as advisory and financial support, as well as business incubators. Business services needed by start-ups differ from those demanded by established enterprises. Unlike established firms, start-ups need more information on how to start a business and on basic accounting and management skills. Start-ups are also more likely to need a working space to start their operations and initial financial support.

Analysis

SME support services

In EaP countries, the market of private business service providers is not very well developed. On the one hand, the market is dominated by international consultancy firms that target large firms which are more profitable and less heterogeneous. On the other hand, business services for small firms are often limited to public support schemes and donor-funded programmes, such as the EBRD's Enterprise Business Growth and Business Advisory Services (formerly TAM/BAS).

Public support for SMEs is most extensive in Armenia and the Republic of Moldova. Currently, the SME support agencies in Armenia (SME DNC) and the Republic of Moldova (ODIMM) provide a wide range of consultancy and advisory services specifically for SMEs in the areas of brand promotion, marketing and personalised services on how to make business plans.

Despite limited private sector involvement, so far EaP countries have not developed a coherent policy framework or action plan on the provision of business services for SMEs. Business support is incorporated into wider SME development initiatives in Armenia and the Republic of Moldova, and is represented by associated measures in annual action plans.

Both have been preceded by an analysis of the market. In the case of the Republic of Moldova, the document is being prepared in consultation with the private sector and is based on a previous detailed analysis of the SME sector and its needs in the Republic of Moldova (OECD, 2011).

Both Ukraine and Belarus have established the regulatory framework for an entrepreneurship support infrastructure, but they lack a strategic approach for the provision of services. Azerbaijan and Georgia have elements of business support provision in their regional development strategies.

Table 7.1. **Scores for sub-Dimension 5a.1: SME support services**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
5a.1.1.	Government action plan on business services	3	1.5	1	1.5	3	1
5a.1.2.	Range of business services	3	2.5	1.5	4	3.5	2.5
Weighted average		***3.00***	***1.90***	***1.20***	***2.50***	***3.20***	***1.60***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Business information for SMEs

The second sub-Dimension assesses the availability and accessibility of business information and the existence of a centralised portal for SMEs to bring together all useful information (and links) for entrepreneurs in one location.

In Armenia, SME DNC and its regional branches play the role of business information centres. They also provide a free reference book containing the contact details of all business services providers. In Belarus and Ukraine this role is taken on by business support centres, registered as such and based on the legislation for small business infrastructure.

Business information can be provided both in physical locations, such as business information centres, and online (through databases, or on specialised websites for SMEs). Using technology to provide information is an important way to make the distribution of information more efficient and less costly both for the government (the information provider) and for the firm. In Armenia, Belarus, Georgia and the Republic of Moldova, extensive business information is available both in paper form at local business information centres and on websites specially designated for entrepreneurs (in the case of Georgia on the website of the Ministry of Economy and Sustainable Development). Moreover, among EaP countries, Armenia, Azerbaijan, Belarus, and the Republic of Moldova have online portals for SMEs that are regularly updated and provide business information, including a list or summary of main business service providers.[2]

Table 7.2. **Scores for sub-Dimension 5a.2: Business information for SMEs**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
5a.2.1.	Business information	4	2	5	5	5	2
5a.2.2.	Quality of online portal	3	3.5	4	2	4.5	1
Weighted average		***3.50***	***2.75***	***4.50***	***3.50***	***4.75***	***1.50***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Support services for start-ups

New high-growth firms are drivers of productivity and employment. While it is recognised that the majority of firms are subsistence-driven and do not have growth ambitions, those that do want to grow and have the potential to do so can drive productivity and employment at the national level (OECD, 2010). Supporting new firms with high-growth potential is therefore an important part of an SME support strategy.

Among EaP countries, several incubators have been set up through donor-funded programmes. However, they are not part of a larger strategic approach. In Armenia, the Enterprise Incubator Foundation was established in 2002 by the World Bank's Enterprise Incubator and is focused mainly on technological start-ups. In Georgia the Batumi Business Incubator was established in 2009 by the local authorities of the Adjara region with the support of the UNDP. In Belarus and Ukraine a wide range of business incubators operate under the law regulating the activities of infrastructure for entrepreneurship support. In Belarus, for example, there were 69 business incubators on 1 July 2011, and 8.5% of the firms located in those incubators were innovative. According to the report of the State Committee of Ukraine for Regulatory Policy and Entrepreneurship (SCURPE) on the implementation of the National Programmes for SME support, on 1 January 2012 there were 10 business incubators, but there is limited information on their effectiveness.

Apart from business incubators, among EaP countries, Armenia is the only country providing a full programme of start-up support. This programme has been carried out since 2004 by the SME Development National Center (DNC) Fund and covers a wide range of services for start-ups (see Box 10.1).

Other available start-up support programmes include Start a Business with the Tbilisi City Hall in Georgia and Pare 1 + 1 in the Republic of Moldova. Both provide grants as well as advisory services to individuals willing to open a business. In the case of Moldova, the programme specifically targets remittances from emigrants who already have a certain amount of capital accumulated from working abroad. In Ukraine the Employment Service provides a lump-sum payment for the unemployed to start a business. However there is no information on the number of businesses that have been started in this way, given that the only condition for payment is the unemployment status of the individual.

Table 7.3. **Scores for sub-Dimension 5a.3: Support services for start-ups**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
5a.3.1.	Business incubators	3	2	3.5	4	4	3.5
5a.3.2.	Advisory services support for start-ups	4	1.5	1	2.5	3	2.5
5a.3.3.	Financial services support for start-ups (vouchers, grants, etc.)	4	1	1	2.5	4	2.5
Weighted average		***3.67***	***1.50***	***1.83***	***3.00***	***3.67***	***2.83***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

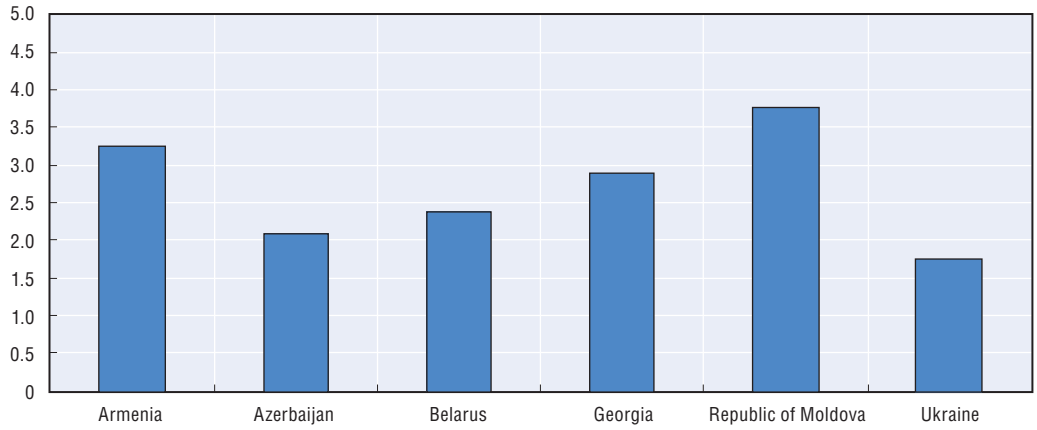
Overall, in EaP countries there is a need for governments to undertake activities to increase the growth capabilities of SMEs by improving their performance in a range of areas such as management skills, adoption of best practices and innovation. Detecting market failures as a first step could ensure that the most important issues are addressed

and the most relevant tools are used for each particular case. In order to identify the areas for support and to avoid distortion of competition, it is important to make a thorough analysis of the market by conducting studies and surveys. International practice must be applied with care, as every country is different, and their SMEs needs may differ depending on their specific economic situation and institutional framework.

The EaP countries are also encouraged to monitor and evaluate their public policy tools on a regular basis to ensure that policy tools are efficient and effective in addressing market failures in business support services (such as training and consultancy services), but also in other areas, to ensure that public budgets are spent with care and that programmes do not create market distortions. The EaP countries still lack mechanisms to assess the effectiveness of their start-up support initiatives, both business incubators and start-up support programmes. One example is monitoring the sustainability and growth of the firms after graduation from the respective programme or incubator. EaP countries are also invited to look into the OECD Framework for the evaluation of SMEs and entrepreneurship policies and particularly the "Six steps to heaven" methodology for assessing the impact of SME policy on companies.

Finally, creating a unified portal covering the entire spectrum of SME-related topics could significantly enhance the accessibility of the business community to information. Online portals are easier to update and can have interactive functions such as forums to discuss new legislative developments or to share problems encountered in business.

Figure 7.2. **Weighted scores for Dimension 5a: Support services for SMEs and start-ups**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

DIMENSION 5B: PUBLIC PROCUREMENT

Introduction

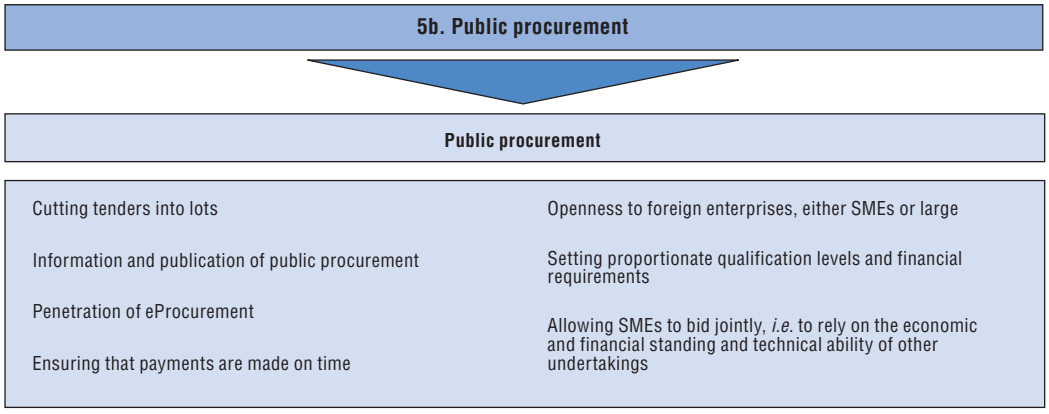
SMEs face more obstacles to accessing public procurement than large firms. While public procurement represents an important source of revenue for firms of all sizes, small firms have less opportunities to benefit from it due to their small size and limited access to information. According to recent research (European Commission, 2010) in EU countries, the share in public procurement that SMEs could secure for themselves in 2006-08 was 14 to 21 percentage points lower than their overall weight in the economy (as measured by combined business turnover), particularly in the case of micro and small firms (European Commission, 2010).

The large size of contracts is generally the most important barrier for SMEs accessing public procurement (European Commission, 2010). Other important barriers are the overly-complicated procedures that have to be carried out just to qualify for the tender. Limited information, lack of clarity on how tender documents are written, and a lack of appropriate debriefing are also obstacles that disproportionately affect SMEs in accessing public procurement.

Assessment framework

Dimension 5b analyses the policies and tools in place in EaP countries to allow SMEs better access to the market of public procurement. The dimension focuses on seven indicators:

Figure 7.3. **Assessment framework for Dimension 5b: Public procurement**



The indicators "Cutting tenders into lots", "Allowing SMEs to bid jointly", and "Setting proportionate qualification levels and financial requirements" allow for assessment of the extent to which public authorities use tools to account for the small size of firms bidding in the tenders and to provide them with equal opportunities.

"Information and publication of public procurement" ensures that information on public procurement is centralised and free of charge for all participants, and there is also training and a helpdesk available to provide informational support for interested firms. "Penetration of eProcurement" measures the existence and implementation of electronic procurement, starting from provision of information on procurement online to the electronic submission of tenders.

"Ensuring that payments are made on time" focuses on the existence of legislation imposing strict deadlines for payments from public authorities, and penalties in case of non-compliance. Finally, "Openness to foreign enterprises", either SMEs or large enterprises, ensures a fair level of competition.

Analysis

According to the responses received, the Eastern Partner countries have made significant progress in several areas. At the same time there are still great divergences across the region. It is not clear whether it is possible to divide tenders into smaller lots in all countries. There is no information as to whether this practice is permitted within the Ukrainian or Moldovan public procurement frameworks.

A visible effort has been made to provide information and publication of public procurement. Generally, information is available, centralised at the national level and free of charge.

E-procurement solutions are in the inception phase, with the exception of Georgia which reported on high level investments in e-procurement solutions. The whole procurement system is designed to operate exclusively through electronic means and this includes tender documentation, tender notices, annual procurement plans, bidding documents and all decisions of the tender commission.

So far, the EaP countries have not developed a coherent policy framework to address late payments, neither in public procurement nor in other areas where one side does not fulfil its contractual obligation. Even though some countries report that late payments are not a problem, this area definitely needs significant improvement. More must also be done on the level of openness to foreign bidders. This domain is particularly problematic in Belarus, where several restrictions are applied limiting access to public procurement by foreign operators.

On the basis of the questionnaires received, it is difficult to draw conclusions on the extent to which public procurement systems differentiate between qualification levels and financial requirements, especially when it comes to SMEs.

Overall, the progress made differs among countries, although significant divergences are visible on individual points.

Table 7.4. **Scores for Dimension 5b: Public procurement**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
5b.1.1.	Cutting tenders into lots	3	3	5	5	1	3.5
5b.1.2.	Information and publication of public procurement	4	4	5	5	3	4
5b.1.3.	Penetration of eProcurement	1	2	1	5	1	1
5b.1.4.	Ensuring that payments are made on time	1	1	1	2	1	1
5b.1.5.	Openness to foreign enterprises, either SMEs or large	4	1	3	5	2	5
5b.1.6.	Setting proportionate qualification levels and financial requirements	1	4	4	3	1	1
5b.1.7.	Allowing SMEs to bid jointly, *i.e.* to rely on the economic and financial standing and technical ability of other undertakings	1	1	3	4	1	2.5
Weighted average		***2.14***	***2.29***	***3.14***	***3.86***	***1.43***	***2.57***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

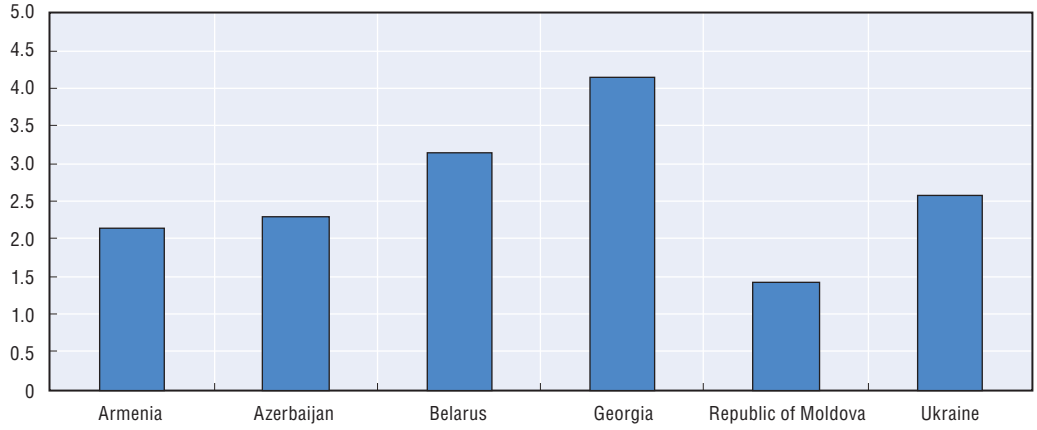
The way forward

Simplification of procedures and requirements for participating in the procurement process could be a first step to support SMEs in participating in public procurement tenders, in particular in the Republic of Moldova. Even though some countries report that late payments are not a problem, this area definitely needs significant improvement. Allowing foreign firms to participate in the bidding could improve competition and hence increase competitiveness of firms.

Countries are encouraged to move toward closer approximation to the EU public procurement standards, which in terms of transparency and non-discrimination can

encourage a general amelioration of the public procurement environment, but also support SMEs by providing more information and transparency to the process of procurement. The countries could refer to the Code of Best Practices (European Commission, 2008), which gives concrete examples on how to promote SME access based on EU public procurement legislation and practices.

Figure 7.4. **Weighted scores for Dimension 5b: Public procurement**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Notes

1. Market systems are not the same in different countries. In particular, in developing countries markets are underdeveloped and in some sectors even non-existent, creating cases where a market economy fails to provide people with a desirable supply of certain kinds of goods and services. Market failures can occur in a market economy when it does not produce enough public goods and goods with positive externalities, when it produces too many goods with negative externalities, when goods are overpriced by natural monopolies, and when market agents do not have access to sufficient information, such as information about the quality of some consumer goods. These market failures usually justify economic intervention by the government. But there is always the risk of government failure – in which faulty political processes or institutional structures prevent government measures from improving social welfare (*source: Beyond Economic Growth. An Introduction to Sustainable Development*, Second Edition, Chapter 11, accessed on *www.worldbank.org* on 4 November 2011, *www.worldbank.org/depweb/english/beyond/global/chapter11.html*).
2. Armenia: *www.smednc.am*; Belarus: *www.svoedelo.by*; the Republic of Moldova; *www.odimm.md*; Ukraine: *www.dkrp.gov.ua*.

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PART II

Chapter 8

Access to finance for SMEs (Dimension 6)

Facilitate SMEs' access to finance and develop a legal and business environment supportive to timely payments in commercial transactions (Small Business Act Principle 6)

Access to finance is one of the main challenges faced by enterprises of the EaP region. According to BEEPS 2009, it is perceived as either the first or the second most important obstacle to doing business. Bank lending, the main source of external funding for SMEs, has been significantly affected by the recent country-specific and international crises. Other external sources of finance such as leasing have yet to be developed.

This chapter focuses on government policies and instruments to facilitate development of and access to external sources of finance by SMEs, according to the Small Business Act for Europe. Dimension 6 contains two main sub-dimensions: sources of external finance for SMEs and the legal and regulatory framework that supports their development. Policies to support general financial literacy, which affects both the demand for credit by SMEs and the supply of finance by financial institutions, is considered in the third sub-dimension.

Introduction

External finance in the form of public support can play an important role in supporting SMEs, particularly start-ups. It can contribute to encouraging and enhancing bank lending to SMEs, especially if such support is efficient and effectively implemented through the private sector. Sustainable development of other sources of external finance for SMEs, such as debt, equity and other financial products (*e.g.* leasing and microfinance) from financial institutions requires the development and effective implementation of a legal and regulatory framework. Improvements in the legal and regulatory environment are important in reducing barriers and stimulating bank lending to SMEs. A functioning cadastre system as well as a central and unified registry for movable assets facilitates the use of land and other assets as collateral for financing SMEs, while the protection of creditors' rights ensures recovery of that collateral in case of default. Comprehensive and accessible credit information systems reduce the information asymmetry between SMEs and financial institutions.

This chapter focuses on government policies and instruments to facilitate development of and increase access to external sources of finance by SMEs, according to the European Union's Small Business Act (SBA). Governments can also contribute to increasing awareness and building the capacity of SMEs to access external finance by helping them understand the different sources of finance and helping them choose suitable modes of financing from the full range of options. They can also help SMEs make themselves more attractive as recipients of non-bank finance.

Assessment framework

The Access to Finance dimension contains two main sub-dimensions and one additional sub-dimension covering other factors that affect the supply and demand of access to finance (see Figure 8.1).

Policies to support general financial literacy which affect both the demand for credit by SMEs and the supply of finance by financial institutions are considered within the third sub-dimension of the access to finance dimension.

Analysis

Access to finance is one of the main challenges faced by enterprises in the Eastern Partner (EaP) countries – on average 18% of SMEs. According to the Business Environment and Enterprise Performance Survey (BEEPS) 2009 of the EBRD, access to finance is perceived on average as the second most important obstacle to doing business by firms in the region (first obstacle in Azerbaijan, Georgia and the Republic of Moldova, and either third or fourth in America, Belarus and Ukraine). The majority of firms across the region perceive access to finance as a moderate to severe obstacle to doing business (from 46% in Azerbaijan to 60% in Belarus and Ukraine). SMEs largely rely on internal sources, which have been negatively affected by the current global crisis and the economic slowdown in the region over the past few years, further restricting SME growth.

Figure 8.1. **Assessment framework for Dimension 6: Access to finance for SMEs**

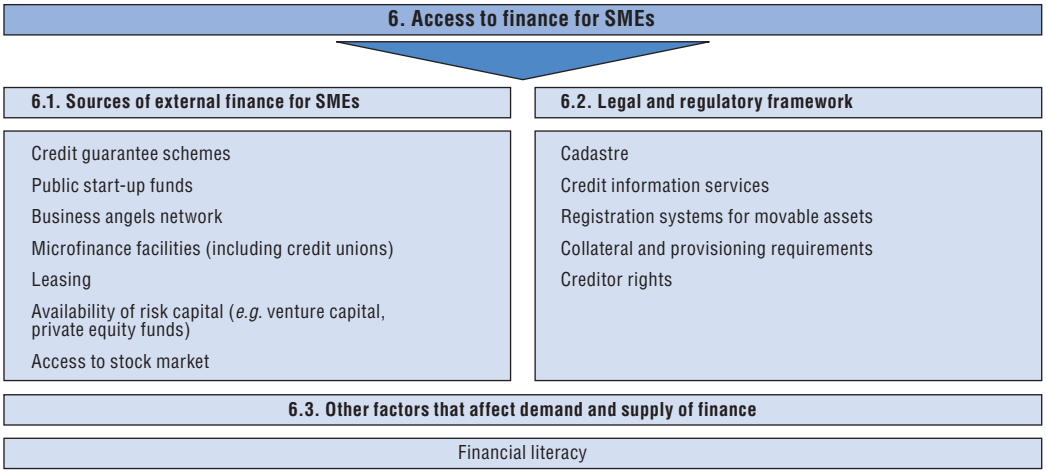
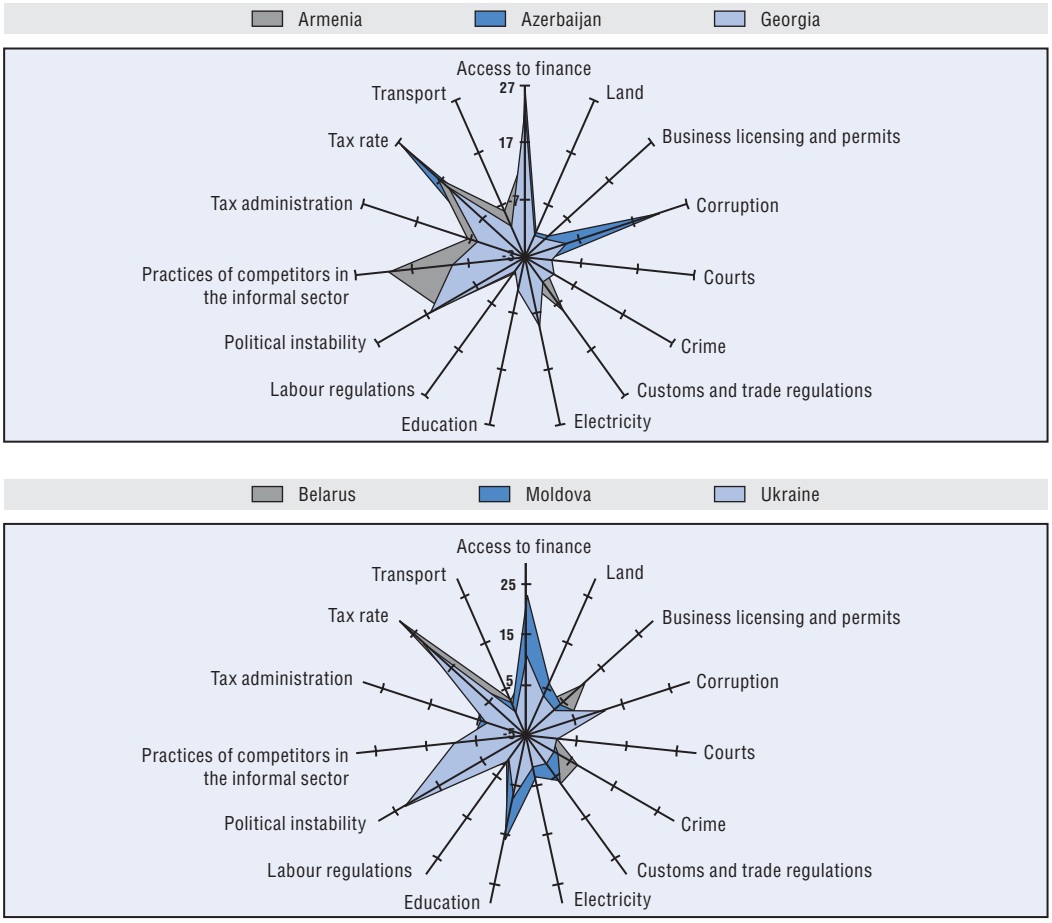


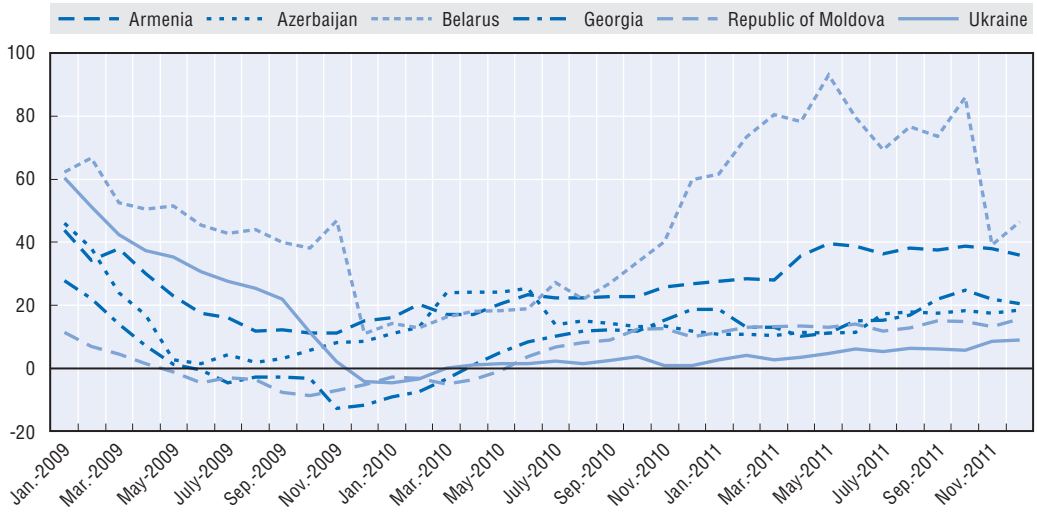
Figure 8.2. **Results of BEEPS 2009 for the EaP countries**



Source: Business Environment and Enterprise Performance Survey (BEEPS), 2009.

According to the BEEPS survey, bank lending accounts for the majority of external financing for firms, accounting for 60 to 90% of external funding (with the remainder coming mainly from supplier credit). This is particularly the case in Belarus and the Republic of Moldova.

Figure 8.3. **Domestic credit growth in the region (in %, 2008-11)**



Note: Belarus' figures include all lending to non-financial sector not only private sector.
Source: IMF-IFS statistics.

However, bank lending remains generally low across the region with domestic credit to the private sector between 18% of GDP in Azerbaijan and 56% in Ukraine in 2011, compared to over 140% of GDP in the EU area. Bank lending has been significantly affected by the global economic crisis. SMEs are especially vulnerable because the risk associated with lending to this sector is deemed by banks to be greater (*e.g.* in terms of insolvency). There was a significant slowdown in credit growth across the region at the beginning of 2009, with the largest drop in Armenia, Georgia and the Republic of Moldova. There was a small recovery in 2010 and 2011 in all countries except Belarus where credit growth decelerated (and declined in real terms) due to the balance of payments crisis. Government support to banks in Armenia counterbalanced somewhat the effect on bank liquidity and lending in 2010-11. Overall, non-performing loans have increased between 2008 and 2009. In some countries such as Azerbaijan and Ukraine this trend has continued into 2011.

Table 8.1. **Banking sector indicators**

	Domestic credit to GDP		NPLs as % of total loans		Asset share of foreign owned banks	Asset share of state owned banks
	2008	2011	2008	2011	2010[1]	2010[1]
Armenia	17.8	32.6	4.4	4.8	67.5	0.0
Azerbaijan	16.5	19.5	2.2	6.4	9.1	41.6
Belarus	28.6	41.7	2	4.5	20.6	77.9
Georgia	33.2	32.8	12.8	8.6	89.3	0.0
Republic of Moldova	36.5	33.6	5.2	9.7	41.5	12.5
Ukraine	73.7	56.0	4.2	16.4	47.8	16.9

1. End of 2008 for Belarus.
Source: WEO, National sources and EBRD banking survey.

Sources of external finance

While bank lending is the main source of external finance for SMEs in the region, it remains insufficient and has been reduced even more due to the crisis. Other sources of finance for SMEs such as leasing have also been affected by the crisis. This is due both to a shortage of funding sources (that often come from banks) and a deterioration in portfolio quality. Government policies and effective public financial support are important to bridge the increased financing gap for SMEs during a crisis. They must encourage bank lending to SMEs amid an increased aversion to risk. Further improvements in the business environment are important for attracting future investors and developing other sources of finance such as private equity finance.

Public support can be used to address market failures and stimulate private sector lending through credit guarantee schemes and start-up support schemes. Such schemes provide soft loans for SMEs requiring less or no collateral. Well-implemented credit guarantee schemes through the private sector can facilitate access to credit by SMEs and can contribute to the integration of small and medium-sized businesses into the financial market. The private sector should play an important role in the implementation of such facilities to ensure that resources are allocated efficiently. However, public financial support in the EaP region has been affected by fiscal constraints. At present, public support by means of credit guarantee schemes is provided through banks in Armenia. In the Republic of Moldova it is provided through the Small and Medium Entrepreneurship Development Centre Fund and the Organisation for SME Sector Development. In Ukraine, credit guarantee schemes are largely under state control and are provided through the state-owned Ukreximbank. In Azerbaijan, the National Fund for Entrepreneurship Support has been providing interest-rate subsidised loans to SMEs through the banking sector since 2004. Credit guarantee schemes are currently under consideration in Belarus and Georgia.

Because banks are reluctant to lend in the absence of a credit history, public start-up funding facilities are essential for the initial development of a business. These publicly-funded schemes are designed to encourage new and growing businesses and may target specific groups of individual entrepreneurs (such as women or young entrepreneurs). Ideally, such funding programmes are self-sustainable and operate throughout the country, providing a wide range of start- up funding products. Start-up funding remains scarce in the EaP region, although some pilot projects have been implemented in the Republic of Moldova (such as the Youth Empowerment Programme) and Armenia. The National Fund for Entrepreneurship Support in Azerbaijan provides special funds to start-ups, mainly targeting women and young entrepreneurs.

Business angels are individuals who invest in start-ups and growing companies in return for an equity stake in the company. Investments by business angels work as a tool used to fill the gap between venture capital and debt finance, especially for start-ups. Government awareness should be raised to promote and/or attract investors in order to develop a competitive business angel network. There is little or no business angel activity in the region, although there has recently been increased government awareness of this activity in Belarus and Georgia. Since November 2010, a Business Angels and Venture Investors Network (BAVIN) is being developed in Belarus. The Georgian government has also completed a pilot project to investigate the functioning of a business angels' environment.

Providers of microfinance for microenterprises often operate within the structure of not-for-profit organisations such as non-governmental organisations (NGOs), credit unions

and other financial co-operatives. They provide different kinds of services including credit, savings, insurance, money transfers and other financial products. Governments can assist the microfinance sector, notably by liberalising banking services in order to facilitate deposit-taking and the long-term sustainability of microfinance institutions (MFIs). They can also regulate the sector, especially in terms of appropriate skills and excessive risk taking. An MFI network is well developed in both Armenia and Georgia and an appropriate institutional structure is in place. According to the Microfinance Information Exchange (MIX), microlending (including by banks) was 6% and 4% of GDP in Armenia and Georgia respectively. However, MFIs in the country lack the necessary capital to meet the demand for microlending. A regulatory framework is in place, except in Belarus where it is still in draft form, and microfinance is available in the other countries of the region, mainly from the state or donor organisations which offer only a limited range of products.

Leasing is an attractive financing tool for SMEs, particularly as a complement to bank loans since it offers uncollateralised lending which is well suited to the needs of SMEs. A fully functioning legal framework and adequate regulation and supervision are both necessary to ensure the proper skills for the development and sustainability of leasing activities. Legislation related to leasing is implemented in almost every country of the region, although a special law on leasing is not in place in Belarus and currently under consideration in Armenia. Leasing activities remain very low and the range of products offered is limited to auto-leasing. Leasing activity in Belarus and Ukraine is the highest among the countries of the region although it represents only 3% of GDP. Leasing of equipment and machinery also remains very low.

Risk capital is an important long-term source of finance for SMEs, both for setting up new businesses and for expanding growing firms. An important and necessary condition for the development of equity capital – in addition to a good general business environment – is the creation of related legislation. It should be in line with best practices of corporate governance and should provide for different exit possibilities. Legislation related to risk capital is undeveloped in Belarus and the Republic of Moldova. In Armenia and Azerbaijan, laws relating to investment funds have recently been adopted. Overall, the use of risk capital is in the early stages of development in the region. Private equity activity is low even in Ukraine, a country that has the most advanced private equity activity in the region, but where the committed equity capital was only 0.5% of GDP in 2010. Venture capital is practically non-existent.

The stock market can also be used as a source of long-term finance for SMEs. A legal framework allowing for the listing of low-capitalised companies could be beneficial to SMEs. Such a framework gives them access to funds outside traditional financing and encourages improvements in the SMEs' profiles and credibility, as well as improving the transparency and corporate governance of the listed entities. Nevertheless, SMEs may have difficulties in participating in listings on stock exchanges, as listings usually entail high costs and a high level of red tape which includes a number of accounting and auditing procedures. The cost of overcoming information asymmetries for SMEs also makes it hard for investors to invest in these small firms. This is particularly notable in EaP countries where the average size of SMEs is small and the SMEs lack financial transparency. However, while stock markets are generally operating in the region, the scope of their activities, outside government securities, is very limited. Market capitalisation ranges between 1.5% of GDP in Armenia and 29% of GDP in Ukraine and markets are not liquid across the region. A generally low level of conformity with corporate governance standards and the lack of a domestic institutional investor base both affect the development of capital markets.

Table 8.2. **Scores for sub-Dimension 6.1: Sources of external finance for SMEs**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
6.1.1.	Credit guarantee schemes	3	2.5	2	2	3	3
6.1.2.	Public start-up funding	2.5	2.5	2	2	3	1
6.1.3.	Business angels network	1	1	2.5	2.5	1	1
6.1.4.	Microfinance facilities (including credit unions)	3	4	2.5	4	3	3
6.1.5.	Leasing	2.5	3	3.5	3	3	3.5
6.1.6.	Availability of risk capital (*e.g.* venture capital, private equity funds)	2	2.5	2	3	2	3
6.1.7.	Access to stock market	2	2	2	2	2	3
Weighted average		***2.29***	***2.50***	***2.36***	***2.64***	***2.43***	***2.50***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Legal and regulatory framework

Public policies for improving the legal and regulatory environment can help stimulate bank lending in general and to SMEs in particular. Developing adequate information systems such as business registration systems, credit bureaus, accounting standards and collateral registries would help to bridge the gap related to the lack of credit information on SMEs. Moreover, the legal environment clearly affects the ability of banks to recover collateral. In this respect, rules which ensure the enforcement of creditor and property rights and adequate bankruptcy laws are the cornerstones of a legal system that facilitate lending to SMEs.

Cadastre is an official register of the quantity, value and ownership of land and real estate. A fully functioning cadastre, easy to access and fully documenting the ownership of land and property is important for the use of land as collateral for SMEs. Overall cadastre systems are in place across the region and the efficiency of their operations has improved in the recent years. Georgia has a fully functioning cadastre launched by the Georgian National Agency of Public Registry (NAPR) and available online since 2007. Online registration services exist in Belarus and the Republic of Moldova. Nevertheless, land ownership has not yet been fully documented in Belarus and Ukraine.

Credit information systems contain data on the credit status of borrowers who are active in a financial system. They help to overcome information asymmetries and to facilitate the pledging of property as collateral by owners of SMEs. Such registers should cover all available credit information. The information should be complete and reliable, as well as widely and easily accessible. Public credit bureaus are usually managed by the central bank, mainly for supervisory purposes, while private credit bureaus are often established by financial institutions. Armenia and Georgia both have a private credit bureau in place, with wide coverage and accessibility. In Azerbaijan and Ukraine credit information services are in place but with access limited to financial institutions only. In Belarus, they are subject to a fee for non-state entities. The private credit bureau was only recently established in the Republic of Moldova.

A central and unified registry for moveable assets also facilitates the use of assets other than real estate as collateral for SME lending, and serves to control the use of the same collateral for multiple loan applications. A registration system for moveable assets is in place and fully functioning in Georgia and the Republic of Moldova. In Georgia it is also available online. Information is hardly accessible in other countries, or is limited to vehicle registration only (*e.g.* Belarus).

Excessively strict rules on the level of collateral and provisioning requirements may constrain bank lending to SMEs. Bank lending remains largely collateral-based and collateral requirements are generally high. Some commercial banks provide more flexible collateral requirements or use guarantees for smaller loans.

Creditor rights refer to the legal provisions in place which preserve the creditors' ability to enforce claims against their debtors. Appropriate legal provisions would establish procedures to settle creditors' claims and would govern the enforcement of rights held by different classes of creditors. A legal environment which protects creditors' rights by providing adequate enforcement mechanisms is likely to be beneficial for bank lending to SMEs, as such rules would facilitate debt collection by creditors. An appropriate legal framework with enforcement of creditors' rights remains a challenge across the region. The legal frameworks on secured transactions in most countries do not fully ensure the necessary rights for secured creditors and their implementation does not guarantee effective collateral recovery in case of default.

Table 8.3. **Scores for sub-Dimension 6.2: Legal and regulatory framework**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
6.2.1.	Cadastre	4	3.5	3.5	4.5	4	3
6.2.2.	Credit information services	5	3.5	2	4.5	2	3
6.2.3.	Registration systems for moveable assets	3	2.5	3	5	4	3.5
6.2.4.	Collateral and provisioning requirements	3	2	2.5	3	2	2
6.2.5.	Creditor rights	2	3	2	3	2	1.5
Weighted average		***3.40***	***2.90***	***2.60***	***4.00***	***2.80***	***2.60***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Financial literacy

Improving general financial literacy is important for both the demand and supply sides of finance to SMEs. The government could help by developing a national strategy that integrates a methodology for evaluating the level of financial literacy and promotes educational programmes. Financial literacy levels are low across the region, as indicated by the generally low level of bank accounts held by the population, and little has been done to develop a national strategy to assess these levels or to promote financial education programmes.

Table 8.4. **Scores for sub-Dimension 6.3: Other factors that affect demand and supply of finance**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
6.3.1.	Financial literacy	2	2	2	2.5	2	3

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Box 8.1. **Legal and regulatory framework in Georgia**

Georgia has significantly improved the legal and regulatory framework that facilitates access to finance for SMEs.

The National Agency of the Public Registry is in charge of the registration of moveable assets in Georgia. Since its creation in 2004, the public registry has undergone successive reforms and has been supplemented with additional functions including online registration of moveable assets in 2009 as well as geodesy and cartography functions in 2011. The online registration system allows for any moveable asset to be used as collateral and thus facilitates access to bank loans by small businesses.

The online pledge registry is particularly beneficial for SME lending given the growing demand for credit by small and medium-sized enterprises. The online pledge registry is centralised and fully operational throughout Georgia.

The following aspects and services are or will be available in the National Agency of the Public Registry:

- Any business may use moveable assets as collateral while retaining possession of the assets.
- Any financial institution may accept moveable assets as collateral.
- The law allows businesses to grant a non-possessory security interest in a single category of revolving moveable assets without requiring a specific description of the secured assets.
- A general description of debts and obligations is permitted in collateral agreements, which allows for all types of obligations and debts to be secured by stating a maximum secured amount in the security agreement rather than a specific amount for each obligation.

Credit information services are provided by **CreditInfo Georgia**. Data relating to credit history are stored on the system for more than two years and are available online. This credit bureau has been active since 2005 when Georgia joined Credit Info, the international provider for credit information. Data on outstanding and repaid loans are provided by the credit bureau. The data are available 24 hours a day, seven days a week. Users can consult credit history through "My creditinfo service". Fees for using the service vary from GEL 15 to 50. Furthermore, a monitoring function automatically alerts users in the event of a change in critical credit information.

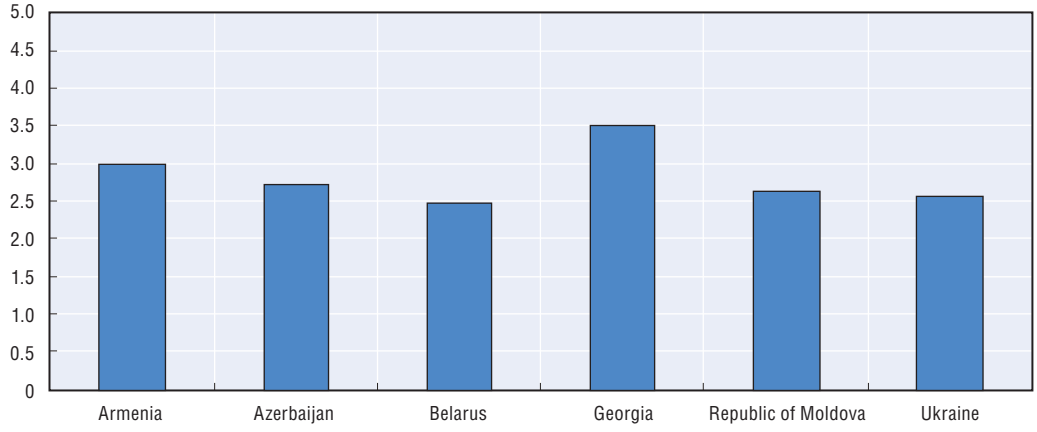
The way forward

Despite improvements, particularly prior to the global economic crisis, access to finance for SMEs remains an important challenge for EaP countries. Bank lending, which is the main source of external funding for SMEs, has been significantly affected by the recent country-specific and international crises. Although there has been some recovery in credit growth in the region since 2010, banks remain cautious about taking risks. The effect of the crisis on the performance of firms and the increase in non-performing loans, in addition to a decline in funding sources and greater uncertainty, have made banks more averse to risk. Slower growth in the region and uncertainties in the Eurozone continue to inhibit credit demand. Although the region is not well integrated financially, a potential disorderly deleveraging of Eurozone parent banks could affect capital inflows, possibly generating a credit crunch in Ukraine where banks rely on parent-bank funding.

Other external sources of finance such as leasing are yet to be developed as an alternative source of finance for SMEs and are also affected by the crisis. Private capital is scarce and equity markets are rather small and illiquid. Public support for SMEs is relatively small and limited by fiscal constraints in most countries (apart from Azerbaijan). Progress in the development of a legal and regulatory framework is heterogonous across countries. While cadastre and credit information systems are developed in Armenia and Georgia, and a unified collateral registry is in place in Georgia and the Republic of Moldova, the enforcement of creditors' rights is generally weak across the region. Financial literacy remains low but recently the government is increasingly aware of this issue.

Enhancing competition and a greater level of sophistication in the banking sector would also benefit SMEs in obtaining access to finance. The funding model for many banks in the region remains a challenge, with a need to develop more local currency sources of funding and longer-term funding. There is increased policy attention to de-dollarisation, and efforts have started to build/strengthen local capital markets. General improvement of the business environment and corporate governance standards is necessary to increase investment opportunities and attract more private equity capital into the region. Building of a domestic institutional investor base (*e.g.* through insurance and pension reform) and related exit opportunities would also help develop equity capital. Reducing the number of administrative procedures and regulations would increase the effectiveness of state financial support. An effective and easily accessible central collateral registry in Armenia, Azerbaijan and Belarus is important for enhancing access to finance for SMEs. The establishment of a private credit bureau in Azerbaijan and Belarus would benefit SMEs by improving information coverage and overcoming information asymmetries. The legal environment which protects creditors' rights by providing adequate enforcement mechanisms for the retrieval of collateral should be strengthened across the region. Increasing knowledge and general awareness of financial issues would also be beneficial to SMEs. For example, it could encourage them to apply for a loan.

Figure 8.4. **Weighted scores for Dimension 6: Access to finance for SMEs**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 9

Standards and technical regulations (Dimension 7)

Help SMEs to benefit more from the opportunities offered by the single market (Small Business Act Principle 7)

Dimension 7 of the SBA assesses the level of progress of Eastern Partner (EaP) countries in eliminating technical trade barriers for industrial and agricultural products. Such barriers can cause severe distortions by preventing market access, protecting domestic producers and discriminating between domestic and foreign producers. Some EaP countries have tariff-free market access to the Single Market through the special incentive arrangement for sustainable development and good governance (GSP+). Today, technical trade barriers still represent one of the most significant obstacles to the liberalisation of trade between the EU and the EaP countries.

Ukraine and Belarus are addressing technical trade barriers for industrial products. The EU completed negotiations on a Deep and Comprehensive Free Trade Agreement between the EU and Ukraine in 2011, implying considerable approximation of legislation in this area. All the EaP countries (except Azerbaijan) have made considerable progress in aligning their sanitary and phytosanitary legislation with the EU framework.

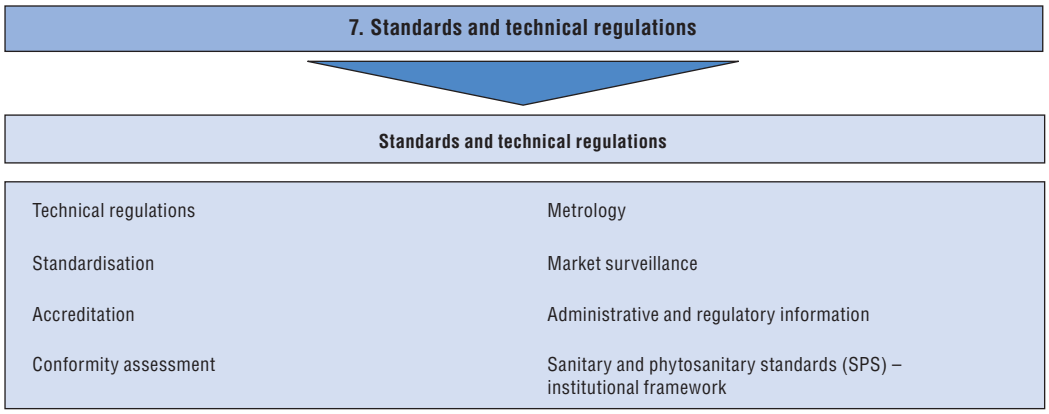
Introduction

Dimension 7, which corresponds to Principle 7 of the Small Business Act (Help SMEs to benefit more from the opportunities offered by the Single Market) is strongly related to the Eastern Partner (EaP) trade agenda: it aims to eliminate technical trade barriers in the area of industrial and agricultural products. Some of the EaP countries have tariff-free market access to the Single Market by benefiting from the special incentive arrangement for sustainable development and good governance – the General Preferential Scheme (GSP+). Today, technical trade barriers are one of the most important obstacles to the liberalisation of trade between the EU and the countries in the Eastern Neighbourhood. Technical barriers to trade can severely distort trade by preventing market access, protecting domestic producers and discriminating between domestic and foreign producers. SMEs in the EaP countries, in particular, must comply with the requirements of the trade-related regulatory environment for industrial and agricultural products. These cover technical regulations, standards, accreditation, conformity assessments, metrology, market surveillance and sanitary and phytosanitary rules.

Assessment framework

The principle has only one dimension, which covers eight indicators:

Figure 9.1. **Assessment framework for Dimension 9: Standards and technical regulations**



Analysis

The EaP region presents a very heterogeneous picture of the development of international and EU trade relations. Belarus and Azerbaijan are still working towards their accession to the World Trade Organization (WTO), while the other four EaP countries (Armenia, Georgia, the Republic of Moldova and Ukraine) have already joined. This is a prerequisite for the EU to consider starting negotiations on a free trade agreement (FTA). At

the beginning of 2012, the European Commission began negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA) with Georgia and the Republic of Moldova. DCFTA negotiations with Armenia are also foreseen to be launched in the course of 2012. In Ukraine negotiations on the DCFTA as part of a future Association Agreement between the EU and Ukraine were concluded in 2011. A customs union between Belarus, the Russian Federation and Kazakhstan is also in force since July 2011.

The trade agenda for EaP countries has also been accompanied by, and is complemented by, the establishment of a panel on Trade and Trade Related Regulatory Co-operation linked to DCFTAs under the auspices of the Eastern Partnership Platform for Economic Integration and Convergence with EU Policies. Various trade panel meetings have been organised by the European Commission to familiarise EaP countries with trade related co-operation in the area of technical regulations as well as sanitary and phytosanitary standards. Importantly, the business community of the EaP countries, which includes SME organisations, has been informed about the requirements of DCFTAs for companies. This was achieved through two business-to-business meetings under the auspices of the trade panel.

Technical regulations

Technical regulations are common, mandatory requirements or rules which govern the composition, manufacturing or marking of a product.

Three of the EaP countries (Ukraine, the Republic of Moldova and Georgia) have already agreed sectoral legislation for at least part of the priority sectors with the European Commission. The technical regulations currently developed for Belarus within the customs union between the Russian Federation, Kazakhstan and Belarus are also harmonised with the corresponding EU directives.

In Armenia and Azerbaijan, sectoral legislation in the priority sectors is in the draft stage.

Standardisation

Standards can be defined as objects or ideas that are authoritative and based on accepted reasons. Standards are shaped – by consensus and voluntarily among enterprises, public authorities, consumers and trade unions – through a consultation process organised by independent, recognised European standardisation bodies at the national and European levels. A harmonised standard is developed on the basis of a request from the European Commission to a European standards organisation to develop a standard providing solutions for compliance with a legal provision.

In the Republic of Moldova, Armenia, Ukraine, Georgia and Azerbaijan, a number of European standards have been adopted and the upgrading of standardisation bodies in accordance with EU requirements has started in several of these countries.

Belarus and Georgia are affiliate members of the European Committee for Standardisation (CEN) and the European Committee for Electrotechnical Standardisation (CENELEC).

Accreditation

Accreditation is a quality infrastructure tool supporting the attestations of conformity assessment bodies both in voluntary and mandatory areas.

Box 9.1. **DCFTA with Ukraine**

In December 2012, Ukraine and the EU completed negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA) as part of a future Association Agreement. The EU is Ukraine's most important commercial partner and accounts for about one third of its external trade. Hence, closer economic integration with the EU will be a key factor for Ukraine's future growth, investment and employment opportunities. It will also create new challenges for Ukrainian and European companies in all sectors of the economy.

Classical trade agreements foresee the mutual opening of markets for goods and services and the abolition of import duties. But these negotiations have gone much further: Ukrainian laws and standards will become compatible with those of the European Union in trade-related areas. This is a very important step towards approximation of legislation.

The agreement implies that Ukrainian manufacturers will meet EU regulations and standards simply by respecting Ukraine's own rules and norms. Coupled with the abolishment of import duties, the barriers and costs of accessing the large market of the EU will further decline.

In Armenia and Azerbaijan, the transposition of EU horizontal legislation and the establishment and/or upgrading of accreditation bodies have just started.

The Republic of Moldova, Belarus and Georgia are affiliate members of the European accreditation system (EA). Horizontal legislation on accreditation bodies has been transposed and an accreditation body (AB) has been established in accordance with EU requirements.

The National Accreditation Agency of Ukraine (NAAU) was created in 2002. Its main functions respond to the requirements of the EA. The NAAU became an associate member of the EA in 2011 and corresponds to the requirements of European and international organisations for accreditation.

Conformity assessments

Conformity assessment is a procedure used to determine that a process, product or service meets relevant technical standards or fulfils relevant requirements. The assessment is carried out before the product is placed on the market and must demonstrate that it fulfils all relevant legislative requirements. The essential objective of conformity assessment is to demonstrate to public authorities that products placed on the market conform to the provisions of the relevant legislation, in particular with regard to the health and safety of users.

In Armenia, Azerbaijan and Georgia, the transposition of EU horizontal legislation on conformity assessment is still ongoing.

In Ukraine, an institutional infrastructure for the assessment of conformity of goods, processes and services based on technical regulations unites a number of bodies which are accredited to the NAAU. However, the level of enforcement requires further improvement and a greater allocation of resources.

In the Republic of Moldova, the national body for conformity assessments (CAECP) works closely with laboratories, inspectorates and institutions to obtain certification. The legislation on conformity assessments is aligned with all EU legislation, legal acts and court decisions (*acquis*).

Belarus has set up a comprehensive and robust national system for conformity assessment. The legal basis for the procedures of conformity assessment was developed according to the corresponding European guidelines and legal acts.

Metrology

Metrology is the science of measurement. Measuring instruments are essential for the accuracy of measurement, notably for transactions by consumers and industry in everyday life such as taxi and electricity meters, weighing machines and the measurement of pre-packaged goods. Units of measurement are essential to ensure the integrity and precision of transactions and to protect health and safety.

In Armenia and Azerbaijan legislation in the area of metrology is still in the draft stage and does not fully comply with EU requirements.

Georgia and the Republic of Moldova continue to upgrade their metrology bodies and institutions in accordance with EU legislation.

In both Ukraine and Belarus, central bodies for metrology are in place and are internationally recognised. Effective operation of the metrological infrastructure is functioning in Belarus.

Market surveillance

The objective of market surveillance is to place only safe products on the community market. In practice, market surveillance comprises a series of interlinked activities and measures carried out by national authorities to ensure that products placed on the community market comply with all requirements set out in the relevant community harmonisation legislation and that those products do not endanger the health, safety or any other aspect of public interest. Market surveillance is organised and carried out at the national level. Each country is responsible for surveillance activities on its territory. This includes taking any necessary action to bring non-compliant products into compliance, to impose restrictive measures (bans or withdrawals) and, if necessary, to apply sanctions.

In Armenia, Azerbaijan and Georgia, legislation in the area of market surveillance is still in the draft stage.

In the Republic of Moldova, a comprehensive system of market surveillance is being developed in accordance with EU requirements. It is directed by the General Division on Quality Infrastructure monitored by the Ministry of Economy.

Ukraine and Belarus have developed a comprehensive market surveillance system in accordance with EU requirements. Furthermore, Belarus is effectively operating its entire market surveillance system.

Administrative and regulatory information

It is crucially important for the governments of the EaP countries to inform their companies of the requirements for export and investment opportunities in the European market. This is particularly true for SMEs which often lack important information in order to successfully access European and international markets.

In the Republic of Moldova, the Moldovan Export Promotion Organisation and the Enterprise Europe Network (EEN) provide information to SMEs on export conditions and opportunities for Moldovan enterprises planning to engage with the EU.

The information process in Armenia is driven by the SME Development Centre of Armenia (SME DNC), the Armenian Development Agency, the EEN and the chambers of commerce, whereas in Georgia, SMEs are informed by the Georgian National Investment Agency.

In Ukraine, Azerbaijan and Belarus, information on export opportunities for companies in the EU is provided by the responsible ministries within the respective governments.

Sanitary and phytosanitary standards (SPS) – institutional framework

The WTO sets regulations on country agricultural policies relating to food safety (bacterial contaminants, pesticides, inspection and labelling) in the form of sanitary rules. Those policies relating to animal and plant health with respect to pests and diseases take the form of phytosanitary rules. SMEs exporting agricultural products in and to the EU must comply with these rules when accessing the Single Market.

Azerbaijan is at an early stage in adopting such legislation. National bodies have been set up, but there are still administrative shortcomings.

In the Republic of Moldova, Georgia, Ukraine, Armenia and Belarus, national bodies are well established, but efforts are still needed to fully align legislation with EU and international standards.

Table 9.1. **Scores for Dimension 7: Technical standards**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
7.1.1.	Technical regulations	2	2	3	3	3	3
7.1.2.	Standardisation	2	2	3	3	2	2
7.1.3.	Accreditation	2	2	3	3	3	4
7.1.4.	Conformity assessment	2	2	4	2	4	3
7.1.5.	Metrology	2	2	5	3	3	4
7.1.6.	Market surveillance	2	2	5	2	3	4
7.1.7.	Administrative and regulatory information	3	2	3	3	5	2
7.1.8.	Sanitary and phytosanitary standards (SPS) – institutional framework	4	3	4	4	4	4
Weighted average		***2.38***	***2.13***	***3.75***	***2.88***	***3.38***	***3.25***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

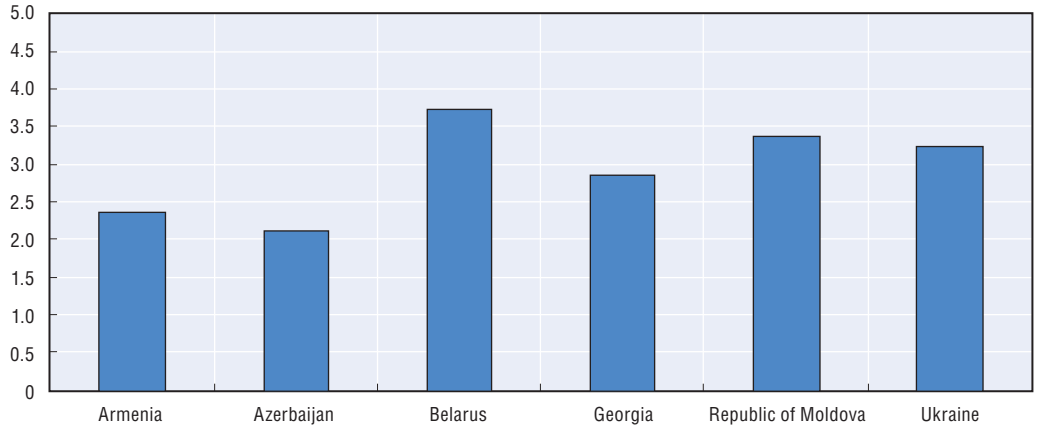
The way forward

As far as technical trade barriers for industrial products are concerned, Ukraine and Belarus are the best performing countries in the EaP region. The EU completed negotiations on a DCFTA between the EU and Ukraine in 2011. This implies that there is already considerable approximation of legislation in the area of technical barriers to trade. In Belarus, the manufacturing sector has traditionally played a much more important role in economic activities than in other EaP countries.

In the area of sanitary and phytosanitary rules, with the exception of Azerbaijan, the EaP countries have made considerable progress in aligning their legislation with the EU framework.

With the exception of the Republic of Moldova, the EAP countries are invited to further improve their administrative and regulatory information aimed at the business community, particularly SMEs, thus addressing their need to comply with the legislative environment of the EU.

Figure 9.2. **Weighted scores for Dimension 7: Standards and technical regulations**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 10

Enterprise skills and innovation (Dimensions 8a and 8b)

Promote the upgrading of skills in SMEs and all forms of innovation
(Small Business Act Principle 8)

Policy makers recognise the importance of innovation and entrepreneurship in today's knowledge-driven economy, and the need to encourage SMEs to engage in innovative activities. The Eastern Partner (EaP) countries need active government support for small business training programmes and entrepreneurial learning, innovation and technology absorption to develop new sources of economic growth.

Principle 8 of the Small Business Act (SBA) provides a framework to analyse and evaluate policies to develop entrepreneurial human capital and support innovation in SMEs. It has two main dimensions: Enterprise skills, and Innovation. The systematic promotion and investment in enterprise training and support through structured policy partnerships and evidence-based policy approaches can anticipate human capital supply needs for the SME sector. The innovation dimension focuses on creating a favourable environment for innovation and technology transfer through institutional co-operation, a strategic approach, establishment of innovation and technology centres and development of technical and financial support schemes for innovative SMEs.

DIMENSION 8A: ENTERPRISE SKILLS

Introduction

This section outlines the assessment framework of the Human Capital Dimension 8 "Enterprise Skills" in the countries of the Eastern Partner region (EaP) and encapsulates the main assessment results on skills policies for SMEs in the region.

As unemployment escalates and economic growth figures decline across the EU and its neighbouring countries, investment in human capital development for national growth, competitiveness and enhanced employability of people is becoming a strong focus for the EU. This is driven by the vision of an intellect-intense and competitive Europe, with similar challenges facing its EU neighbours. Hence, the Small Business Act for Europe (SBA) strives to overcome "structural difficulties such as the lack of management and technical skills, and remaining rigidities in labour market at national level" (European Commission, 2008a, p. 7). The EU2020 policy perspectives for human capital underline the importance of entrepreneurship support and emphasise skills improvement as a factor for increased employability and the creation of new jobs. The low relevance of traditional education and the rigidity of response from education systems to the changing demands of the labour market make school-to-work transition extremely difficult. This leads to high youth unemployment and places growing emphasis on diversification of types and forms of learning, flexibility and adaptability of learning providers, development of supply-demand matching tools, etc. It also requires new approaches to empowerment of the learners by providing them with the competences necessary for self-employment, equipping individuals with an ability to learn throughout their lives, seek opportunities and be creative, adaptable and entrepreneurial in all aspects of their careers and social life.

Considering these challenges, governments and their social partners are seeking out policies, institutions and tools to assure a quality diagnosis of the skills situation in their countries and to carry out support measures and create the conditions that would be particularly conducive to SME human resource development. Producing quality data and analysis is a key element of any policy needs assessment, and is equally important for monitoring progress in policy implementation and evaluating the impact of specific policy measures which address the skills development and upgrading of SMEs. Experts call for measures to generate knowledge about SMEs, and above all the "structural requirements and specific characteristics of their future skills needs. Without such knowledge, their outstanding contribution to employment and wealth in Europe and their role as a driving force for innovation and economic growth both nationally and internationally are endangered" (FBN, 2011, p. 17).

Transitional and developing countries are considering the EU's policy approaches and practices for supporting SMEs in the context of their own reforms, and when addressing their own economic and social challenges. They are also considering competitive pressures in a time of global crisis. Countries of the EaP region are calling for effective policy instruments and

tools to address the impact of structural mismatches between supply and demand, to increase the effectiveness of government measures and public investment in raising productivity, to improve the quality of the labour supply relevant to the demands of tomorrow's economy and to reduce the skills gaps both for wage-earners and the self-employed. In the countries of the EaP region, increased pressures on the education and training system call for a new type of interface between the government, training providers and employers and other social partners. On the one hand, employers, especially in the micro, small and medium-sized enterprise sector, gradually become conscious of the importance of training, mentoring and support for the sustainability and growth of enterprises. On the other hand, education and training providers need to focus on ensuring the relevance of the content and the format of proposed training services, based on a systemic analysis of the training needs of their clients – SMEs, both in their start-up early phase and during their growth. While large enterprises, mainly state-owned, generally have been able to sustain the tradition of on-the-job retraining, professional development and upgrading of workers, small enterprises have few opportunities and limited resources to organise such retraining. Thus systemic co-operation with the government and business support organisations and pooling the individual efforts of enterprises to support training for SMEs would represent a strategic investment into the future growth and success of small enterprises.

Countries of the EaP region face the dilemma of modernisation within their education and training systems in the context of their social and economic transition. At the same time they are responding to the demands of the free market and building awareness among their citizens of the high value of entrepreneurship and self-employment as a worthwhile career choice. The first SBA policy assessment offers a window of opportunity for the region to draw the attention of its society to the need for systematic promotion of and investment in enterprise training and support. This can be achieved through structured policy partnerships and by introducing evidence-based policy approaches to anticipate the human capital supply needs of the SME sector.

Assessment framework

The Enterprise Skills assessment framework has been developed jointly with experts from the EaP countries, based on the key principles of the SBA. It is consistent with the set of indicators applied in previous assessments in the EU pre-accession region. Thus it ensures continuity of the policy review methodology, assessment process, and comparability of results across the European Union's neighbouring regions. It also creates a strong basis for cross-border policy learning, contributing to enhanced co-operation and the exchange of knowledge, expertise and good practice among partner countries of the European Union.

While in the other regions the follow-up SBA policy assessments allow for tracking of national progress, the first policy assessment in the EaP region is helping to establish a baseline for further systemic monitoring and evaluation of national policy developments. It thus contributes to the promotion of evidence-based policy-making.

The set of enterprise skills indicators applied in the first assessment in the EaP region consists of five indicators: training needs analysis (TNA), access to training, quality assurance, start-up training and enterprise growth. Most indicators are process-oriented and qualitative, with the exception of one quantitative indicator ("start-ups") and the quantitative elements in the "enterprise growth" indicator. While the battery of five indicators represents a comprehensive policy matrix covering the complexity of issues in the human capital policy development agenda with relation to the SME sector, each of the

five indicators is used as a separate assessment unit and selectively addresses the key aspects of effective national policy or practice: availability of training, its relevance to SME needs, the quality of the actual training provided, the targeted character of training and support for both new and growing enterprises. Each indicator is designed in such a way that the process of evidence collection for the assessment stimulates policy learning among the stakeholders involved and fosters their co-operation around the key elements of policies: data collection needs and instruments, collaboration in strategic networks, quality assurance systems and approaches, specific measures and institutional support structures for various types of enterprises, etc.

Training needs analysis (TNA)

The training needs analysis (TNA) indicator looks at the establishment of a national policy and support framework to ensure a better fit between supply and demand for training in small enterprises. It was designed with the assumption that public and private investment in training is more cost-effective when the training offer reflects the specific demands of the market. In a medium-term strategy perspective, this indicator promotes dialogue between the government, SME training providers and their clients – small and medium-sized enterprises – in anticipation of their current and future skill needs. It also stimulates collaboration among training providers and fosters networking and better definition of roles and functions in the training market. In addition, it ensures the systematic implementation of measures and tools for establishing a comprehensive national framework of TNA to identify skills weaknesses in the workforce, skills gaps and future skills requirements.

Access to training

The Access to training indicator reflects the importance of the policy focus on availability of a well developed training market as an important precondition for access to training by SMEs to enhance their business performance. It is designed to stimulate expansion of the offer of training services for SMEs in a manner that is balanced across the territory of each country of the EaP region. It also ensures that such services are available both in rural and urban areas, and that the information about the training and support opportunities is equally accessible to all enterprises irrespective of their location.

Quality assurance (QA)

The Quality assurance (QA) indicator determines the importance of enhancing the quality of skills development to strengthen enterprise confidence in the training market and to create further demand for skills upgrading – both management and trade skills – in the SME sector. It leads to the development of a more competent workforce, well equipped to face the demands of the modern labour market. The purpose of this indicator is to trigger policy decisions and implementation measures in each country of the EaP region. This would result in the introduction of a transparent quality assurance system for SME training programmes and training providers, and would fully align part of the national education and training QA framework with European principles and standards for education and training.

Start-up training

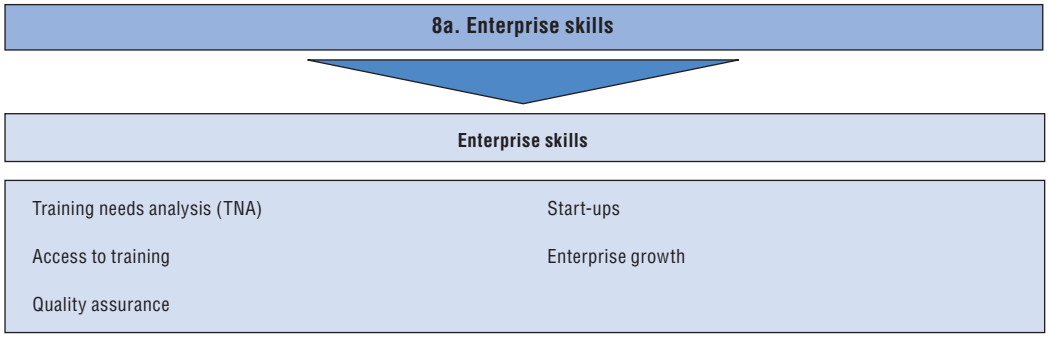
The Start-up training indicator reflects the importance of the availability of targeted training and mentoring services for start-up enterprises. It is assumed that fine-tuned start-up training and mentoring encourages the creation of new ventures and contributes

to positive start-up survival dynamics. This indicator serves as a "policy barometer" indicating whether start-up training is included in the focus of the government's SME policies. It presumes that start-up training is among the government's priorities, that a budget is available and that statistical data have been collected for monitoring the scope of training provision. This is a quantitative indicator that implicitly focuses on the policy measures in the countries of the EaP region on strategic development of disaggregated government statistics allowing transparent monitoring of the availability of pre- and postHstart-up training and support services. This indicator focuses mainly on ensuring that the first steps of entrepreneurs in establishing new ventures are supported by "entrepreneurial literacy" training and mentoring, thus radically improving the survival chances of newly-established enterprises. Availability of online/e-training has been given special weight within this indicator due to its importance for the flexible delivery of training services.

Enterprise growth

Similar to the Start-ups indicator, the Enterprise growth indicator stimulates the implementation of dedicated support measures, the availability of ear-marked state funding and systemic monitoring tools for impact evaluation of training programmes for growth enterprises. Positive dynamics of growth, innovation and internationalisation within the SME sector increase the overall productivity and competitiveness of the economy. All these have a substantial impact on national economic performance indicators. Training and support measures for high-growth enterprises substantially differ from those for newly-born enterprises. Training for new enterprises aims to develop basic skills and competences to enable new business ventures to be launched and sustained. A substantial portion of high-growth enterprises' activities are knowledge-intense and require human resource development focuse on skills for innovation, new products and services, internationalisation, expansion into new markets, etc., thus contributing to exponential job creation and wealth generation. Governments need to make this type of SME support a strategic priority, with a dedicated policy framework, a public resource base and a support infrastructure.

Figure 10.1. **Assessment framework for Dimension 8a: Enterprise skills**



Analysis

At present, no country in the EaP region has a well established national training needs analysis (TNA) framework that encompasses the systematic collection of data on the training needs of the SME community. Analysis of training needs of enterprises is

conducted mostly on an *ad hoc* basis in all countries of the EaP by surveys of training providers, employer organisations, career guidance programmes and employment services, projects for SME support, donors, etc. In Georgia, Armenia, Azerbaijan and the Republic of Moldova, government, social partners and the business community have engaged in dialogue to establish a systematic training needs analysis framework for SME training. In the Republic of Moldova this process is triggered by discussions on the development of the new National SME Strategy. In Ukraine and Belarus there are interesting examples of project-driven skills intelligence while system-driven policy actions are still to be defined along the SBA framework recommendations.

In addressing the Access to training indicator, all countries of the EaP region have policies and dedicated institutional structures in place, as well as state-funded implementation measures for SME training, business consulting and financial and information support to small enterprises. However, in most cases, the availability of these services is limited to specific towns and regions. Evidence of an online register of training providers and programmes broken down by region has been found in Armenia, Azerbaijan, Belarus, the Republic of Moldova and Ukraine where training provision is envisaged under the priorities of national strategies or programmes for economic development, SMEs and entrepreneurship support. In Armenia, government funding has been allocated for the development of online training courses for SMEs. Georgia, Azerbaijan and Belarus have gone one step further and already offer distance learning programmes for SMEs.

Though no country of the EaP region has an operational national quality assurance system, Georgia has made progress on voluntary accreditation of public and private training providers through the National Centre for Educational Quality Enhancement (NCEQE). In all EaP countries, international accreditation of individual training courses and *ad hoc* application of quality assurance tools and instruments have been identified. Some examples are implementation of client satisfaction surveys by training providers and assessment of the outcomes of training for small enterprises. Ongoing development of the National Qualifications Frameworks in some countries (Azerbaijan, Ukraine) also has a triggering effect on the definition of quality standards of training provision for the SME sector. While no accreditation of business training providers is implemented in Armenia, in Belarus all educational and training providers are subject to state accreditation. Government and business support institutions in Ukraine accredit training providers and place information on the relevant regional and national websites.

Concerning start-up support, overall, no country in the EaP region has been able to provide sufficient statistical evidence on the ratio of start-ups trained and/or those that received business support services during the assessment period. Therefore, the assessment scores are based on indirect evidence. Government statistics are fragmented in all countries and – in most cases – are not collected along the parameters of this indicator. A non-government segment of enterprise training provision is not monitored at the national level. Some countries collect data on training services provided to priority groups of clients. The Republic of Moldova monitors provision of training for young entrepreneurs, returning migrants, etc. Armenia and Belarus collect statistics on the overall numbers of state-supported training courses for SMEs, without tracking the start-up segment. In Georgia, the state voucher system in vocational education and training (VET) supports individual and group training within both public and private providers. In most cases, governments, public and private training providers and social partners have yet to combine

their efforts in systemic monitoring of the availability of early training, mentoring and business support services for start-up enterprises with the aim of improving their coverage and access

Box 10.1. **National Centre for SME Development in Armenia**

In 2004 the National Centre for SME Development (SME DNC) of Armenia launched an innovative "Start-up business support program" which has now been successfully implemented and further developed. The programme is based on a CEFE methodology introduced jointly with the GIZ. It envisages a multi-stage, comprehensive support programme offered to participants for at least one year.

The programme provides co-ordinated and comprehensive access to a range of start-up support instruments and services – information provision, training, consulting and mentoring, in combination with effective financial instruments – which leverages the use of resources and increases the effectiveness of individual government support measures for new entrepreneurs in the Republic of Armenia.

SME DNC includes the selection of participants, provision of training and support to the development of business plans by the trainees, their access to targeted financial support (loans with subsidised interest rates, loan guarantees, etc.) and offers various forms of follow-up support: coaching, group and individual consulting, etc. To date, more than 1 000 participants have been trained in the framework of 63 training campaigns in various regions of Armenia. Before 2012 only 25% of graduates of the programme registered their own businesses. Since the beginning of 2012 the proportion grew to 50%-60% due to the new approach adopted by SME DNC. Currently the start-up campaigns are adjusted to separate industry sectors and target groups, including women and youth, allowing the application of approaches tailored to their specific needs.

The programme has a regional focus and is financed as part of the government's support targeting regional unemployment and boosting productivity and sustainability of small enterprises in the Republic of Armenia.

Within the Enterprise growth indicator, state budget support to training and business advisory services for high-growth enterprises is available in Georgia and is linked to the criteria allowing growing enterprises to apply for subsidies to support training and advisory services. In Armenia development of the knowledge and skills needed for enterprise growth is a priority in the national economic development plan and state financing. In Azerbaijan, Belarus and the Republic of Moldova state support to training, infrastructure development, information and business consultation services for high-growth enterprises is carried out within the general framework of SME development.

Table 10.1. **Scores for Dimension 8a: Enterprise skills**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
8a.1.1.	Training needs analysis (TNA)	2	2	1	2	2	2
8a.1.2.	Access to training	2.5	3.5	2.5	3.5	2	2.5
8a.1.3.	Quality assurance	2	2	2	3.5	1	3.5
8a.1.4.	Start-ups	2	2	2	2	2	2
8a.1.5.	Enterprise growth	2.5	2	2	3	2	2
Weighted average		***2.13***	***2.19***	***1.69***	***2.69***	***1.75***	***2.44***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

The availability of state-supported and private enterprise training and business support institutions in all countries of the EaP region, as well as the existing legislative and regulatory base, will allow each country to move forward on practically all aspects of the assessment framework of Dimension 8a.

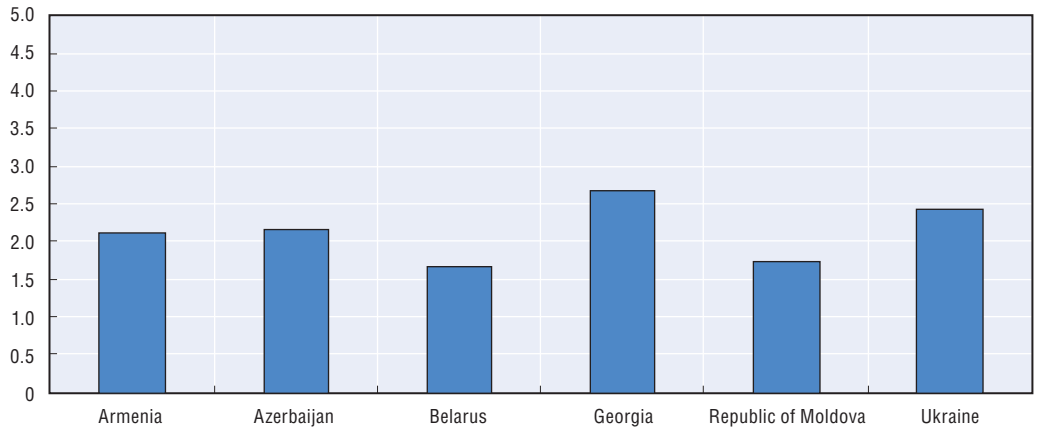
A policy partnership between the business community, training providers and government is needed for national co-ordination at all levels, for implementation and monitoring of enterprise training and for support measures. This requires post-SBA national policy dialogue to continue among the main stakeholders – the business community, training providers and government. They must agree on how to jointly implement policy measures to ensure the availability of training and support services for SMEs in a way that is balanced across the territory of each country, both in rural and urban areas, in the centres and in distant regions. They must also be available in a variety of forms, such as online training courses, help lines, etc. A structured policy partnership would require setting up strategic priorities supported by the allocation of an ear-marked budget and an agreement among all stakeholders on the division of roles and responsibilities for implementation and monitoring of jointly developed policies.

The development of national quality assurance systems for enterprise training should benefit from an existing basis of licensing and accreditation in the systems of formal education and be linked to national strategic discussions on the definition of education quality. It should focus on the quality of both inputs and outputs of training for the small business community. In the countries working towards the establishment of national qualifications frameworks or those already advanced on quality assurance systems in individual parts of the education system all these important initiatives need to be co-ordinated and mutually reinforcing for the development of national quality assurance frameworks. In any case, it is important to plan with both a medium- and long-term perspective and ensure a broader overview of all elements that are instrumental for achieving high quality inputs and outputs in the lifelong learning paradigm. The quality assurance systems should cover aspects of quality standards, policies and procedures, institutional capacity and internal QA mechanisms, competences of teachers and trainers, certification, licensing and accreditation, etc. Quality assurance mechanisms should be designed to cover various parts of the learning system, including private training provision and the diversity of non-formal learning types.

Targeted policy actions are needed for the training and support of start-up and high-growth enterprises. SBA assessment discussions with stakeholders in the EaP countries have provided a recommendation to public and private training providers, social partners and government ministries responsible for entrepreneurship, SME education and training policies: to join their efforts in systemic monitoring of the availability and co-ordination of early training, mentoring and business support provision to new enterprises and to improve coverage and access. Furthermore, special focus is placed on support to enterprises with high growth potential, establishment of institutional and regulatory frameworks for implementation of comprehensive training and financial and advisory support measures for growing enterprises. The business community and the government must agree on the criteria for linking up training, advisory and financial support measures in all countries of the EaP region.

Regular and systematic data collection on the training needs of small enterprises is an important part of an evidence-based policy monitoring culture. The data structure and quality should be guided by the policy monitoring needs. It must be embedded in national statistics and provide inputs for the development and monitoring of national economic strategies.

Figure 10.2. **Weighted scores for Dimension 8a: Enterprise skills**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

DIMENSION 8B: INNOVATION POLICY FOR SMEs

Introduction

Innovation and technology absorption are widely recognised as a fundamental driver of economic growth in both advanced and emerging economies. Innovation activities are also a vital source of productivity, job creation and a catalyst for providing novel solutions to social needs and challenges. In the Eastern Partner (EaP) region, countries are looking for ways to revitalise their economies in response to the global financial and economic crisis. In this context, well designed policy interventions may be used to support technology absorption, transform lagging industries and develop new sources of innovation-led growth.

According to the OECD Oslo Manual, innovation entails the development of new or significantly improved products, processes, marketing or organisational methods (OECD and Eurostat, 2005). This definition reflects the growing understanding that innovation is not just limited to research and development (R&D); rather, it encompasses a broad spectrum of knowledge-driven activities that ultimately lead to the growth of output and productivity. The relationship between innovation and technology absorption is curiously symbiotic: innovation allows for companies to increase their capacity to absorb external knowledge and technologies. At the same time, the application of existing technologies at the firm level can also serve to inspire new ideas and innovations (World Bank, 2011).

There is an increasing awareness among governments of the vital contribution of SMEs to the innovation process. However, due to their limited size and capacity, small businesses often face difficulties in developing and sustaining innovative activities. In the EaP region, private sector investment in innovation is also constrained by a legacy of publicly owned R&D institutes, which continue to dominate the market, restrict SME access to R&D funding and deter SMEs from participating in collaborative research projects and ventures.

Faced with an increasingly competitive and interconnected global environment, governments have an important role to play in fostering the growth of innovation in SMEs. Developing innovation support services, strengthening links between research centres and SMEs, and facilitating the development of clusters are just some of the ways in which policymakers can assist SMEs to develop their innovative capacities. With regard to innovation policy, the Small Business Act encourages governments to undertake the following activities:

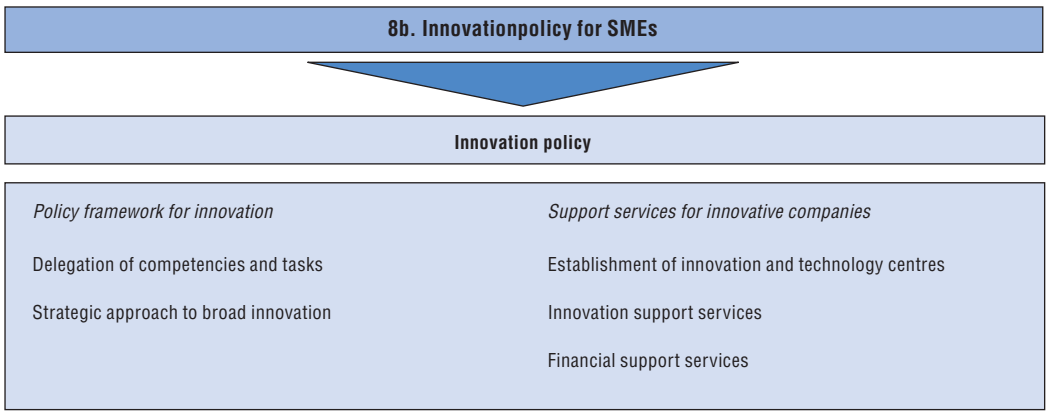
- Strengthen programmes to promote innovative clusters and networks and support high-growth enterprises (particularly SMEs).
- Ensure simplified access to public research infrastructure and national research programmes and active participation of SMEs in trans-national research activities.
- Foster innovative activities and the commercialisation of knowledge through the development of financial and non-technological support services for small businesses.

Assessment framework

The OECD Innovation Strategy recommends that countries treat innovation "as a central component of government policy, with strong leadership at the highest political levels" (OECD, 2010a). Innovation should be integrated with the policies of different departments and agencies, including entrepreneurship, environmental and education policies. Achieving policy coherence and co-ordination is difficult but necessary to encourage all forms of innovation, reduce structural inefficiencies, avoid overlapping of policy actions and harmonise local, regional, national and international efforts (OECD, 2010b). Indeed, the effective organisation of innovation support programmes and institutions can allow for constructive and practical exchanges between relevant stakeholders, leading to the fulfilment of constructive policy actions to promote innovation and entrepreneurship.

Governments can create a favourable environment for the growth of innovative enterprises through the development and implementation of a comprehensive innovation strategy, covering a number of core public policy objectives. In particular, a strategic approach to fostering innovation may be used to unite policies that drive innovation in a mutually supportive manner. Moreover, the development of a strategic approach to innovation policy may be used to develop and co-ordinate programmes to foster public-private partnerships (PPPs), financial support schemes and innovation support services.

Figure 10.3. **Assessment framework: Innovation policy for SMEs**



Analysis

Eastern Partner countries need to increase institutional co-ordination for innovation policy and develop a strategic approach to fostering innovative SMEs

Innovation policy is still in its infancy in the EaP region, and a well-structured policy framework for innovation is lacking in most countries. A comprehensive innovation strategy is a necessary first step for all countries in the region. In Belarus, strategic documents covering innovation policy need to be followed up with concrete policy actions to secure increased participation from SMEs in innovative activities. Ultimately, the development and implementation of a sound innovation strategy will lead to the implementation of policy instruments to promote innovation and encourage increased co-operation between the private sector, government and universities and research institutions.

Eastern Partner countries would benefit from the development of targeted support services for innovative SMEs

Direct measures to foster innovation and technology transfer in SMEs are of key importance in the EaP region. Most countries have developed targeted policies to encourage further involvement of SMEs in the innovation process, with mixed results stemming from the implementation of pilot projects and support schemes.

A well functioning network of innovation and technology centres can be used to engage SMEs in the innovation process, by fostering links between government, industry and academia. In the EaP region however, innovation and technology centres are often faced with numerous barriers which prevent them from effectively fulfilling their role. In the Republic of Moldova, for instance, limited public funding for innovation and technology centres has led to an over-reliance on donor-funded initiatives. In Belarus and Ukraine, state-owned research and development institutes continue to operate as standalone entities, discouraging private sector participation in collaborative R&D activities. Active policy measures are also needed to ensure that innovation and technology centres are able to create links and facilitate co-operation between SMEs, universities and public research institutes.

Financial and technical support schemes for innovative companies are largely provided on an *ad hoc* basis in the EaP region. As a result, SMEs typically find it difficult to finance innovative ventures, and access to consultancy, training, and business support services is limited. In Belarus, a number of publically-funded financial and technical support schemes are in place. However, state-owned enterprises are typically the primary beneficiaries of these support schemes, and private sector participation is extremely limited.

Table 10.2. **Scores for Dimension 8b: Innovation policy for SMEs**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
8b.1.1.	Delegation of competencies and tasks	1	1	3	1.5	2	3
8b.1.2.	Strategic approach to broad innovation policy	2	1	3	2	2	2
8b.1.3.	Establishment of innovation and technology centres	2	2	2	2	2	2
8b.1.4.	Innovation support services	2	1	2	2	2	2
8b.1.5.	Financial support services	2	2	3	2	2.5	2.5
Weighted scores		***1.79***	***1.29***	***2.83***	***1.91***	***2.13***	***2.37***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

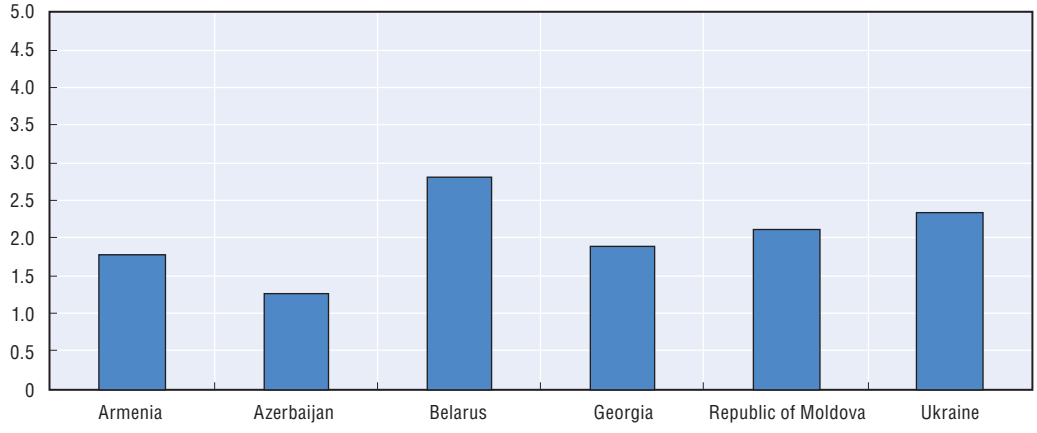
Innovation systems in the EaP region have considerable scope for further development. In the wake of the recent global financial and economic crisis, well-designed policy measures may be used to restructure public R&D institutes, develop targeted innovation support services, and introduce a range of financial instruments to support collaborative ventures and stimulate private sector involvement in innovative activities.

As a necessary first step, EaP countries should develop a co-ordinated approach to the development of innovation policy, including active measures to promote innovative SMEs and high-growth enterprises in various sectors of the economy. A broad and inclusive innovation strategy is also needed, with active measures to promote private sector participation in publicly funded research projects. In addition, public funding can be used to promote social entrepreneurship as a source of innovative solutions to social problems and challenges.

In order to stimulate innovation and further encourage risk taking, EaP countries would benefit from the introduction of targeted support services and financial instruments for innovative SMEs. These programmes, in particular those funded by governments, would encourage greater private investment in R&D, address market failures constraining private investment, and reduce SMEs' reliance on donor-funded initiatives. The introduction of targeted measures to raise the absorption and innovation capacity of SMEs should be synchronised with the introduction of an incentive structure in the education and research area which bring the skills of workers, employees, managers and owners of SMEs to the level required for production means, *i.e.* machinery and organisational innovation. Such an incentive structure would furthermore be conducive to trustworthy contract research, collaboration between public research institutions and the private sector, and the secondment of researchers to private companies.

Finally, efforts should be made to establish links between SMEs and publicly funded research institutions, and to develop a network of innovation and technology centres that regularly interact and co-operate with SMEs. Such an interaction could also help to develop the necessary technical and organisational skills for SMEs to effectively apply technical standards.

Figure 10.4. **Weighted scores for Dimension 8b: Innovation policy for SMEs**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 11

SMEs in a green economy (Dimension 9)

Enable SMEs to turn environmental challenges into opportunities
(Small Business Act Principle 9)

Principle 9 of the Small Business Act assesses the approaches of governments to fostering green growth and strengthening the absorptive capacities of SMEs. It assesses current strategies for "greening" concepts, the availability of expertise on environmental issues to SMEs, the use of environmental management system (EMS) and standards, and governments' efforts to promote EMS. SMEs will be able to benefit from green growth opportunities if they adjust their business models accordingly. Governments can support SMEs to change their practices and adapt to the challenges by "greening" their current strategies in the field of SMEs, industry and innovation and by promoting a policy framework for eco-efficient business and products as well as supporting eco-innovation.

Introduction

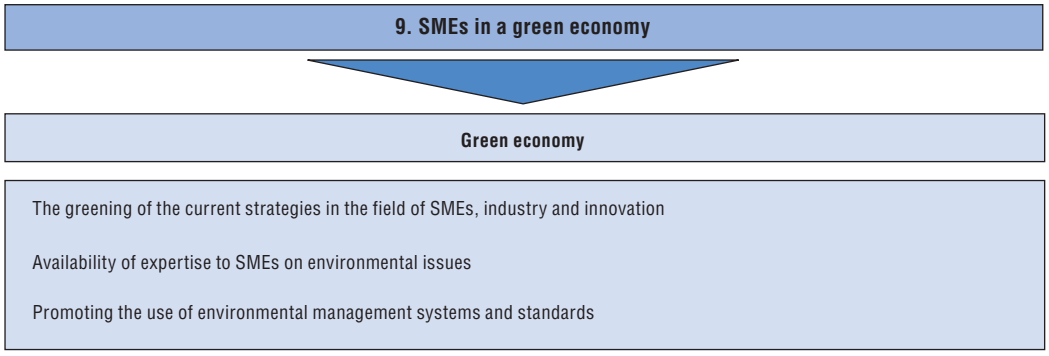
In many EU and OECD countries, increasing emphasis is now placed on the sustainability of SME legislation and policy initiatives, notably in the area of environment and climate change. SMEs will be able to benefit from green growth opportunities if they adjust their business models accordingly. Governments can support SMEs to help change their practices and adapt their businesses to the challenges by "greening" their current strategies in the field of SMEs, industry and innovation through the promotion of a policy framework for eco-efficient business and products as well as eco-innovation.

Assessment framework

Principle 9 of the Small Business Act (SBA) assesses governments' approaches towards fostering green growth and strengthening the absorptive capacities of SMEs. The principle has only one dimension, which is based on three indicators:

- The "greening" of current strategies in the field of SMEs, industry and innovation examines whether strategic enterprise and innovation policy documents cover eco-efficiency and eco-innovation. It assesses the extent to which these concepts are embedded in national policy frameworks.
- The availability of expertise on environmental issues to SMEs evaluates the availability of environment-related information and expertise available to SMEs.
- The promotion of the use of environmental management systems and standards measures governments' efforts to promote environmental management systems and standards.

Figure 11.1. **Assessment framework for Dimension 9: SMEs in a green economy**



Analysis

In addition to the Trade and SME Panel, an Environment and Climate Change Panel has also been established under the auspices of the EaP Platform on Economic Integration and Convergence with EU Policies, reflecting the priority this area has been given by the Eastern

Partner (EaP) countries with respect to regional economic co-operation. Despite political declarations, framework strategies and policies aimed at sustainable consumption and production have yet to be developed. Among the possible reasons are the low priority given to green growth issues on the political agenda, weak inter-sectoral and inter-ministerial co-ordination, fragmented economic decision making in specific policy areas and a lack of appropriate information.

It has been agreed that this dedicated panel would co-operate closely with the SME Panel on environment and climate change matters, particularly regarding the promotion of green technologies and eco-innovation. The SME Panel should serve as an important tool to assess the impacts on SMEs in the EaP countries of recommendations issued by the Panel on Environment and Climate Change and report back to the latter.

Within the activities of the Panel on Environment and Climate Change, a study on Opportunities and Options for Promoting a Green Economy in the Eastern Partner Countries was completed in 2011. It analysed the capabilities of the countries to implement eco-innovative policies and green economy principles. Furthermore, the European Commission envisages the preparation of a regional project on Sustainable Development and the Green Economy which will be introduced in the SME Panel.

Greening of current strategies in the field of SMEs, industry and innovation

In the Republic of Moldova, no reference has yet been made to eco-efficient business and product innovation in the policy framework.

As far as Azerbaijan, Belarus, Georgia, Armenia and Ukraine are concerned, green economy concepts are being taken into consideration in strategic government documents.

However, so far clear mechanisms to promote these strategies for SMEs have not been developed.

Availability of expertise to SMEs on environmental issues

SMEs are often ill-informed about environmental issues. They also tend to lack the in-house capacity to successfully address these issues. Governments can therefore play a crucial role in facilitating access to both environmental information and expertise.

Information on environmental legislation and policy frameworks is available in all the EaP countries and is mainly delivered by the government.

In Georgia and Belarus information and environmental support is also provided by NGOs.

However, in all countries these activities are not co-ordinated at the national level and no specific funding for SMEs is available.

Promoting the use of environmental management systems and standards

Environmental management systems (EMS) and standards provide businesses with a means to systematically improve their environmental performance and advertise their environmental achievements (*Introductory Guide to EMAS*).* ISO 14001 and the EU EMAS – which has recently been extended to organisations outside of the EU – are the most

* Institute of Environmental Management and Assessment (*www.iema.net/ems/downloads*).

commonly used EMS standards. Governments can support the adoption of such standards through awareness-raising activities, direct financial support and incentives.

With the exception of the Republic of Moldova, the governments of the EaP countries provide information on environmental management systems (EMSs) and in some countries, a number of companies have already been certified by EMS standards.

Specific funding for the implementation of EMSs for SMEs is not available in any of the EaP countries.

In Belarus, companies with certified EMSs enjoy tax incentives.

Box 11.1. **Promotion of environmental management systems (EMS) in Belarus**

The Republic of Belarus actively promotes the certification of EMSs in accordance with ISO 14001 requirements. Information on environmental certification is widely available and also integrated in procurement rules. Moreover, the companies with a certified environmental management system enjoy specific tax incentives: According to the Tax Code of the Republic of Belarus (Article 207, Clause 3, Subclause 3.3), enterprises may apply a 0.9 coefficient to environmental tax amounts within three years after receipt of the conformity certificate.

Table 11.1. **Scores for Dimension 9: SMEs in a green economy**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
9.1.1.	The "greening" of the current strategies in the field of SMEs, industry and innovation	2	2	2	2	2	2
9.1.2.	Availability of expertise to SMEs on environmental issues	3	3	4	4	3.5	3
9.1.3.	Promoting the use of environmental management systems and standards	3	3	4	3	1	3
Weighted average		***2.57***	***2.57***	***3.14***	***2.86***	***2.14***	***2.57***

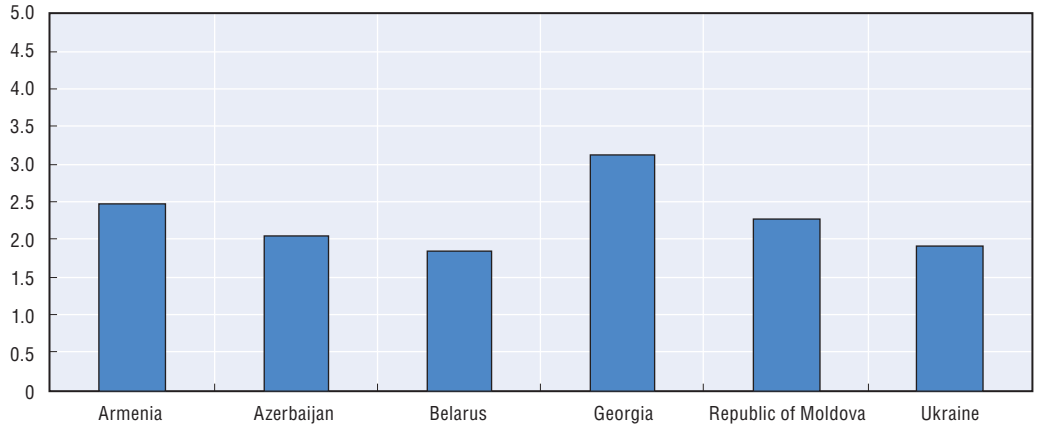
Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

With the exception of the Republic of Moldova, concepts of green economy and eco-efficient business and innovation have been taken into consideration in the government policy frameworks of all EaP countries. The business community is mainly informed by the government on these issues. In some of the countries, companies have been certified by EMSs, but specific funding for SMEs with respect to the promotion of eco-efficient business and green economy is not available in any of the countries. Advice on solutions to comply with the environmental regulations could be given by private and public innovation advice and support services providers, notably research organisations. Land-use planning schemes may be designed in a way so as to facilitate an environmentally friendlier way of operating in SMEs through a consultative process between planning authorities and business associations.

A corrigendum has been issued for this page. See http://www.oecd.org/about/publishing/Corrigendum_EaP_SME_PI_page%20171.pdf

Figure 11.2. **Weighted scores for Dimension 9: SMEs in a green economy**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

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PART II

Chapter 12

Internationalisation of SMEs (Dimension 10)

Encourage and support SMEs to benefit from the growth of markets
(Small Business Act Principle 10)

Enterprises are under increasing pressure from globalisation and the constraints of domestic markets, and the internationalisation of their activities is crucial so as to benefit from the growth of markets. Internationalisation can bring many advantages to SMEs, such as increased productivity by being exposed to competition outside the country, better management practices and a larger market for their goods, as well as creating a wider business network. SMEs can also grow and achieve economies of scale which cannot be reached when operating in the domestic market alone. Nevertheless, only a small percentage of SMEs are involved in exporting activities relative to their share in local and regional economies. To help SMEs tap into external markets, governments should provide support to encourage them to export. This chapter focuses on government activities in promoting exports by SMEs.

Introduction

Under the increasing pressure of globalisation and the constraints of domestic markets, enterprises consider internationalisation[1] of their activities to be a crucial step towards benefitting from the growth of markets. Small enterprises are being confronted with the challenges of a globalised, highly competitive economy where innovation, technology and the ability to serve consumer needs drives market success. In the Eastern Partner (EaP) countries in particular, SMEs quickly learn that domestic markets provide limited opportunities for growth (this is less true for Belarus and Ukraine). Expansion outside the nation's borders thus becomes a natural goal for a growing SME.

Internationalisation can have many advantages for SMEs. By being exposed to competition outside the country, firms are pushed to be more productive through innovation and the adoption of technology in order to be able to compete with other firms. Small firms also get the chance to be exposed to international best practice and to create a wider business network. Finally, by entering the global market, SMEs can grow and achieve economies of scale which cannot be reached when operating in the domestic market alone.

Despite these numerous advantages, only a small percentage of SMEs are involved in exporting activities, compared to their share in local and regional economies. According to the OECD Measuring Entrepreneurship Indicators, SMEs (firms with up to 250 employees) contributed between 20 to 70% of exports in their countries in 2007, and the share of exports by SMEs is higher for smaller countries.[2]

In order to help SMEs to tap into external markets, many governments put in place programmes to encourage exports. Generally, there are informational, administrative and technical barriers to enter external markets. Most of these barriers will affect SMEs disproportionately due to their limited resources, weaker management skills and lack of information. Government programmes should therefore be directed towards providing those skills and knowledge which are most needed by SMEs.

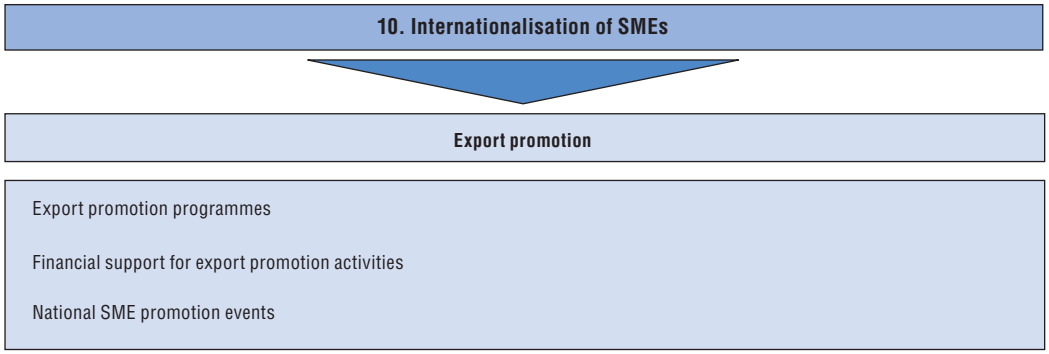
Assessment framework

This principle consists of one single dimension which is made up of three indicators covering several aspects of export promotion for SMEs (see Figure 12.1).

Analysis

To encourage businesses to export, government programmes can provide support in the following areas: financing, improvement of the business environment, capacity building and access to information and markets. Most existing export support programmes both in OECD and EaP countries belong to the last category. Moreover, member countries of the World Trade Organization (WTO) – Armenia has been a member since 2003, Georgia since 2000, the Republic of Moldova, 2001 and Ukraine 2007[3] – are not allowed to directly subsidise their export activities. However the government may indirectly support firms by providing information and training, as well as financing export promotion activities.

Figure 12.1. **Assessment framework for Dimension 10: Internationalisation of SMEs**



In the European Union, several governments support the internationalisation of SMEs, *e.g.* by providing financial support for export promotion, market access strategies and participation in trade fairs (Cyprus, the Czech Republic, Denmark, Estonia, France, Germany, Ireland, Italy, Latvia, Lithuania, Malta, the Netherlands, Poland, Portugal, the Slovak Republic, Spain, Sweden and the United Kingdom). Some of them (*e.g.* Denmark, Slovenia) focus on high-growth companies willing to internationalise; others have established new export promotion agencies (*e.g.* Luxembourg) or new support programmes (*e.g.* Hungary). A mentoring scheme, whereby large companies support the internationalisation of SMEs, is also being piloted (*e.g.* France) (European Commission, 2011).

In Poland, in particular, the measures include subsidies for obtaining product certificates, for publishing promotional materials, and for trade promotion programmes. Other forms of promotional activity include funding consultancy to evaluate export market opportunities, export credit services and information for SMEs on export markets (via a website) (OECD, 2010).

As in the case of business services, the support needed by SMEs that are not yet exporting is different to the support needed by those that have already entered the exporting arena. Firms that are not yet involved in exporting find it harder to access information on the markets, their specific demands and potential business partners. They also find it difficult to make strategic plans for entering markets. Firms that are already in the exporting market on the other hand, are more interested in developing their marketing skills and creating a reliable business network (OECD, 2008).

Export promotion activities are sometimes integrated into investment promotion. The two areas have many synergies and often investment attractiveness depends on the exporting capacity of a country. This role is usually taken by an agency with the specific role of implementing investment and export promotion programmes.

In the EaP countries, Armenia, Georgia, and the Republic of Moldova have agencies that specialise in promoting exporting firms:

- The Armenian Development Agency (ADA) provides support for participation in international trade fairs, provides market information to exporters, carries out trainings and promotes Armenian products on foreign markets. Moreover, the Export Promotion programme within SME DNC provides information and specialised advise on internal exporting procedures as well as requirements for exporting specific products. It also carries out training courses for upgrading skills in international trade, marketing,

management, finance and negotiations. It has also published the Exporting Roadmap, which is available on its website.

- An Export Promotion unit was created at the end of 2010 within the Georgian National Investment Agency (GNIA) within the Ministry of Economy and Sustainable Development. The unit provides information on legislation, trade regimes, export procedures, etc. to firms interested in exporting and organises workshops and seminars.
- Moldovan Investment and Export Promotion Organisation (MIEPO) is the agency within the Ministry of Economy responsible for export promotion activities and implementation of the strategy aimed at attracting investments and promoting exports (2006-15). The activities of MIEPO are mainly focused on the organisation of international exhibitions and fairs, where SMEs are usually well represented. The organisation also provides information on exporting procedures.

All three agencies provide financial support to exporting firms by allocating subsidies to firms that want to participate in trade fairs. For example ADA covers up to 50% of costs for firms located in Yerevan and up to 80% for firms located in other regions. Moreover, in Armenia the Export-led Industrial Strategy, in force since 2012 and implemented by ADA, aims to promote exports through a strategic approach in prioritised sectors based on public-private partnership mechanisms.

The Export Promotion Department within the Azerbaijan Export and Investment Promotion Foundation (AZPROMO), a joint public-private initiative, aims to strengthen and expand the non-oil export capacity of the country. However, the agency does not primarily target SMEs in its activities of export promotion support. In addition, an action plan "On export promotion of non-oil products in 2011-13", co-ordinated by the Ministry of Economic Development, envisages the improvement of the business environment for foreign trade activities in the non-oil sector. Among its plans are the building and strengthening of export infrastructure as well as several targeted measures, such as spreading awareness, education of entrepreneurs in the fields of quality management in enterprises, organising forums and other campaign activities.

Belarus and Ukraine have no specialised agency for export promotion. However, Belarus has a National Program for Export Development for 2011-15 and Ukraine has an Action Plan to Support Export Activities of Small and Medium Business Entities for 2009-11. No funds have been allocated to either of these plans, both remaining only on paper.

Table 12.1. **Scores for Dimension 10: Export promotion**

		Armenia	Azerbaijan	Belarus	Georgia	Republic of Moldova	Ukraine
10.1.1.	Export promotion programmes	2.5	3	2	3	2.5	2
10.1.2.	Financial support for export promotion activities	3	1	1.5	3	1.5	2
10.1.3.	National SME promotion events	1	2.5	2.5	4	4	1.5
Weighted average		***2.50***	***2.07***	***1.86***	***3.14***	***2.29***	***1.93***

Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

The way forward

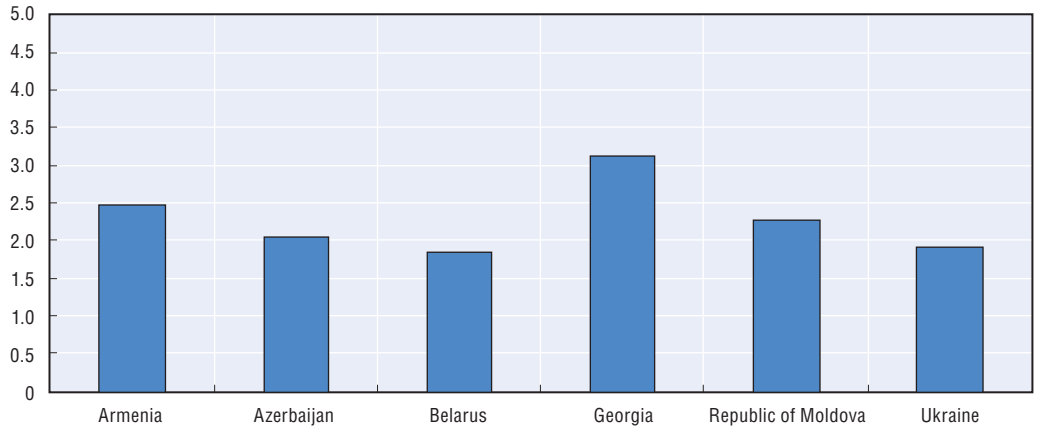
Export promotion agencies in the EaP countries could further improve the capabilities of domestic firms to compete internationally by improving their access to trade finance

and export insurance, assisting them in obtaining creditworthiness, rating potential international partners, providing international market information, fostering research and development and implementing international quality standards.

Creating greater awareness of exporting as a growth and market expansion opportunity can give a boost and increase the interest of firms in exporting. However, information is limited. Greater awareness could lead to overcoming the barriers arising at various stages of the exporting process.

Finally, it is crucial that all the export promoting activities of various government and non-government agencies are co-ordinated in order to avoid overlap and reach maximum efficiency. All countries should set up monitoring and evaluation mechanisms to make it easier to assess the effectiveness of export promotion programmes.

Figure 12.2. **Weighted scores for Dimension 10: Internationalisation of SMEs**



Source: Small Business Act assessment conducted in Eastern Partner countries (2012); see Scores and Methodology for further information.

Notes

1. Apart from exporting and importing, internationalisation may include other activities such as subsidiaries, branches or joint ventures abroad.
2. *OECD Trade by Enterprise Characteristics Database*, extracted on 29 August 2011 from OECD.Stat.
3. Azerbaijan and Belarus have observer status, their working parties having been established in 1997 and 1993, respectively.

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PART III

Eastern Partner country profiles

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PART III

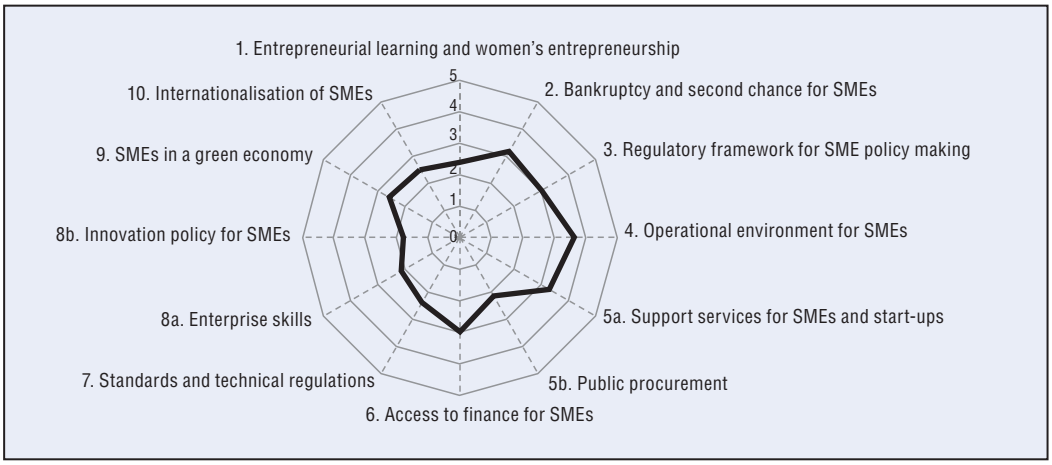
Chapter 13

SBA country profile: Armenia*

Since 2000, the Armenian government has pursued a pro-active approach to supporting SME growth. Key developments were the establishment of an SME policy implementation agency, creation of an SME Support Council and, currently, work on a new SME strategy. Armenia has achieved the highest scores in the areas of operational environment as a result of recent and extensive deregulation initiatives. The SME Development National Center Fund (SME DNC Fund), an efficient and geographically far-reaching SME agency, offers effective SME support tools such as business services and training and information centres, particularly for start-ups. Armenia further supports SMEs in building its export and innovation capabilities. Despite these improvements and the government's declaration that SME development is a strategic priority, the sector still needs a strong and viable development strategy and effective policy implementation mechanisms. According to the SBA assessment, key areas which should be given priority are SME financing, innovation and export promotion.

* This chapter was prepared with the support of EV Consulting and Tereza Khechoyan.

Figure 13.1. **SBA scores for Armenia**



Note: The scores for each dimension are calculated based on assigned weights for each indicator (see Annex A for further information).

Overview

This section provides a brief economic snapshot and highlights some recent trends in the business environment. This is followed by a detailed overview of the current situation of the SME sector in Armenia.

Economic snapshot

Armenia is a small, landlocked, mountainous country with a total population of more than 3 million, most living in urban areas (64%). The country is facing a severe outflow of labour, mainly highly educated university graduates (8.8% of tertiary educated professionals in 2000). In 2010, approximately 28% of its population lived abroad, ensuring a continuous flow of remittances to the country – approximately 9% of GDP in 2010 (WB, 2011).

Despite strong economic growth, Armenia's unemployment rate remains high (7% of the total population in 2010[1]). The agriculture sector is the largest source of employment (45.3% in 2010) (Armstat). Both agriculture and the construction sector, the two sectors most severely affected by the crisis, remain the largest in the Armenian economy, accounting for 17% of GDP each (Armstat).

The country continues to rely heavily on external financing to sustain its large trade deficit. In 2010, the deficit reached USD 2.2 billion, approximately 24% of GDP, the largest among Eastern Partner (EaP) countries. Remittances and transfers from abroad helped to offset about one third of the deficit. As another important source of external financing, foreign direct investment (FDI) reached slightly more than half a billion USD in 2010 (UNCTAD).

Business environment trends

The country has made significant progress in improving its business environment. Its latest improvements are the implementation of a one-stop-shop system to facilitate business registration, and simplification of taxation procedures. These improvements moved the country from the 61st to 55th position in the 2012 World Bank *Doing Business* report.

Table 13.1. **Armenia: Main macroeconomic indicators, 2008-12**

Indicator	Unit of measurement	2008	2009	2010	2011	2012 (proj.)
GDP growth	Per cent, y-o-y	6.9	–14.1	2.1	4.7	4
CPI inflation	Per cent, average	9	3.4	8.2	7.6	4.3
Government balance	Per cent of GDP	–1.8	–7.7	–4.9	–2.7	–3.1
Current account balance	Per cent of GDP	–11.8	–15.8	–14.7	–12.3	–11
Net FDI	USD million	940	725	562	590	620
External debt	Per cent of GDP	29.5	56.4	65.6	65.5	66.7
Gross reserves	Per cent of GDP	12.1	23.2	20	18.2	18.3
Nominal GDP	USD billion	11.7	8.6	9.4	10.1	10.5

Source: EBRD (2011), data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks.

Despite these improvements, an EBRD survey of economies in transition showed Armenia to have the lowest proportion of successful business starters (3.5%) (EBRD, 2011). A large number of firms still perceives practices of the informal economy, tax administration and political instability as major obstacles to business growth (World Bank and EBRD, 2009). Economic activity is largely concentrated in the capital city, Yerevan, as the quality of public infrastructure and services in the rural and border areas is very low. Other issues that hinder business development are corruption and anti-competitive practices in key sectors of the economy (*e.g.* import of some commodity products such as sugar, butter, fuel).

The unfavourable geographical location and the small size of the internal market represent additional challenges, especially for SMEs, as businesses rely heavily on international trade opportunities in order to grow and develop. However, these are undermined by a poor infrastructure network and borders closed to neighbouring countries.

SMEs in Armenia

The SME sector contributes considerably to Armenia's economy. The sector experienced robust growth in parallel with the country's rapid economic development until 2008. However, the global economic crisis has deeply affected this sector's performance, which was particularly vulnerable to the crisis. Following a contraction of about 10% in the volume of production in 2009, the sector has not yet regained its pre-crisis performance level.

Table 13.2. **Definition of micro, small and medium enterprises in Armenia**

	Micro	Small	Medium
Before 01.01.2011			
Headcount	≤ 5	≤ 50 in industry and other productive spheres ≤ 25 in construction and power engineering; science and education ≤ 15 in transport, trade and services	≤ 100 in industry and other productive spheres ≤ 50 in construction and power engineering; science and education ≤ 30 in transport, trade and services
After 01.01.2011			
Headcount	< 10	< 50	< 250
Annual turnover	≤ AMD 100 m (EUR 0.2 m)	≤ AMD 500 m (EUR 1 m)	≤ AMD 1 500 m (EUR 3 m)
Annual balance sheet total	≤ AMD 100 m (EUR 0.2 m)	≤ AMD 500 m (EUR 1 m)	≤ AMD 1 000 m (EUR 2 m)

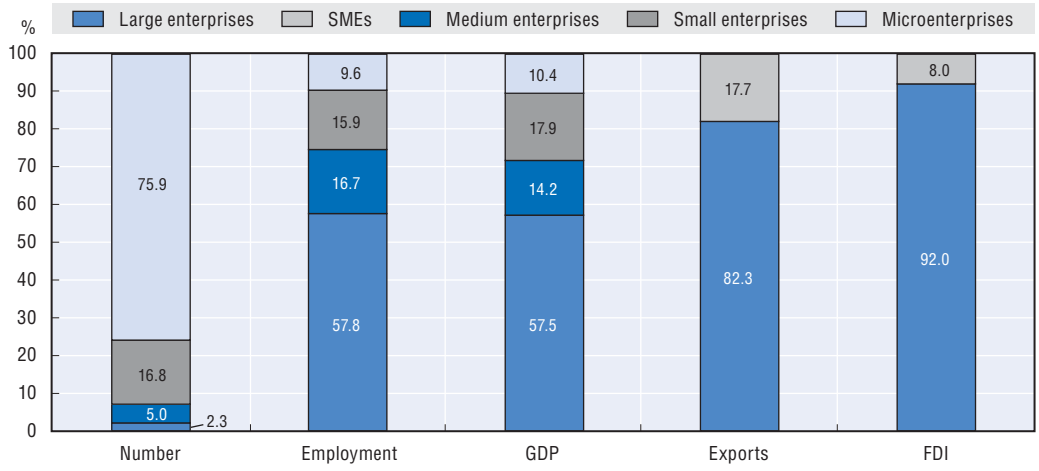
Source: Law of the Republic of Armenia On State Support of Small and Medium Entrepreneurship amendments from 5 October 2010 to the Law of the Republic of Armenia On State Support of Small and Medium Entrepreneurship, in force since 1 January 2011.

Based on the definition of SMEs in force up to 2011 (see Table 13.2), in 2009 the total number of registered SMEs in Armenia was 132 923, which represents 97.7% of total registered legal entities and sole proprietors (136 008).[2] Even though microenterprises represent a large proportion of SMEs, since 2007 their share has decreased from 82.6 to 75.9%, while the share of small and medium-sized enterprises has increased (SME DNC, 2010).[3]

Approximately half of the registered SMEs operate in Yerevan, Armenia's capital city, where the density of SMEs is 55.4 firms per 1 000 inhabitants, compared to 33.3 in other regions of Armenia.

In 2009, the contribution of the SME sector to the GDP was estimated at 42.5%[4] and accounted for approximately 42.2%[5] of total employment in Armenia. While limited in industry (30.6%) and transport and communication (28%), the share of GDP stemming from SMEs is substantial in trade (49.4%), services (45%) and construction (37.2%). Microenterprises in particular account for more than 20% of value added in the trade sector.[6]

Figure 13.2. **SME sector in Armenia, 2009**



Note: The data are based on the old definition applied before 2011 (see Table 13.2).
Source: SME DNC (2010).

Even though SMEs contribute significantly to the economy, both in terms of GDP and employment, their role in attracting FDI and their contribution to exports are very small, revealing the underlying problem of lower competitiveness of SMEs in comparison with larger companies. Thus, in 2009, only 8% of FDI was directed towards SMEs, while exports by SMEs represented only 17.7% of the total. Both figures have remained almost constant since 2007.

The informal economy, which is not covered in the official statistics, represents a significant part of Armenia's economy, and concerns mainly SMEs. According to the latest estimates of the Asian Development Bank, it represented 11.3% of the total GDP in 2009 (ADB, 2010). According to the same source, the contribution of the informal sector to the gross value added is the highest in agriculture (22.4%),[7] construction (15.4%) and wholesale and retail trade (14.8%), the sectors with the largest SME share.

SBA assessment results

This section outlines the main results for Armenia from the 2012 SBA policy assessment of EaP countries.The assessed policy dimensions were reassembled and grouped under five wider SME policy areas.

Strengthening institutions and mechanisms for SME policy making

Armenia follows a pro-active SME policy approach with functioning mechanisms for SME policy making already in place. To further strengthen their effectiveness, the country is currently revising its SME development strategy. The private sector's views are taken into consideration through a process of public-private consultations. The government is committed to reviewing and simplifying legislation with an impact on SMEs and has recently adopted a legal framework for regulatory impact analysis (RIA).

Institutional framework

Armenia is following a pro-active SME policy approach with a number of institutions and policy tools in place to support the growing SME sector. The Ministry of Economy (formerly the Ministry of Trade and Economic Development) and the Small and Medium Entrepreneurship Development National Center Fund (SME DNC) are Armenia's main institutions responsible for SME development:

- The Ministry of Economy develops SME policy, which is based on the Law on State Support and the Concept for SME Development Policy and Strategy (2000). A Medium-Term Financial Programme is developed every three years and an Annual State Programme for Small and Medium Entrepreneurship State Support includes a detailed list of projected initiatives with implementation timelines.
- SME DNC Fund implements the annual action plan and operates as a well-established unit with a clear mandate and organisational structure. Other relevant entities (ministries, organisations, etc.) are consulted in the process to ensure alignment and policy co-ordination. Despite the 2010 budget cut, with the fund's state support being reduced about four times which adversely affected the enlargement of its operations, SME DNC has accumulated funds for financial support, reaching approximately AMD 629 million (EUR 1.3 million) for loan guarantees and AMD 142 million (EUR 0.3 million) for start-up financial support. However, additional financial resources will be required to sustain operations and the implementation of SME support measures in the future.

Clearly, the government of Armenia is committed to fostering SME sector development as one of its strategic priorities, but financial funds for well developed tools and good practice examples of SME DNC are still not available. As the economic realities in Armenia have changed, a new SME strategy, which is being developed, will replace the Concept for small and medium entrepreneurship development policy and strategy in Armenia (2000).[8] The new strategy aims to create a globally competitive SME sector through better business education, access to finance, policies targeting SMEs, improving public-private dialogue and establishing links between SME development policy and other policy objectives. The strategy also has clear targets in terms of the contribution of SMEs to GDP and employment. Adequate financing for SME DNC and a clear political commitment for SME support initiatives are additional key factors required for successful implementation of the strategy.

In 2011, Armenia also switched to a new definition of SMEs in accordance with EU criteria, marking the importance for the country of international comparability. However, the limited availability of data and the change in definition hinder the capacity of policy makers to accurately assess the situation and measure the progress of the SME sector, and hence to develop relevant measures for its development.[9] Improvement in the quality and quantity of data concerning the SME sector, which can be collected through specialised statistical agencies (in this case by the Armenian Statistical Agency), is an important step towards a strong evidence base for SME policy.

Legislative simplification and regulatory impact analysis (RIA)

Armenia has embarked on an extensive programme to reduce obsolete business-related legislation and simplify regulation. In December 2010, the Ministry of Economy approved an action plan for reforms in key areas of the World Bank's *Doing Business* report (*e.g.* paying taxes, starting a business, trading across borders). In addition, a dedicated council has been established and given responsibility for undertaking the legislative guillotine process, with financial support and technical assistance from international organisations.

The government of Armenia has recently adopted a legal framework for RIA, but so far its impact is limited. The adopted RIA calls for a preliminary assessment of the potential impacts of draft legislation through cost-benefit analysis, and consultations with stakeholders from SMEs and industry. While this is a positive step towards a better understanding of the policy impact on business, the impact of RIA on legislation is not evident, which means that this new instrument is not yet well developed and its effect is still limited. To address this, the Ministry of Economy is working as a centralised system for impact assessment on SMEs, competition and other policy areas. Integration of the EU guidelines for the SME test within the legislative framework for RIA, as well as the inclusion of *ex post* analysis of the impact of new laws and regulations on SMEs, could further improve the existing mechanism.

Public-private consultations (PPC)

Despite a solid legislative background, public-private consultations (PPC) in Armenia must be further improved. In 2000, a Business Support Council was established as a main body for public-private dialogue. It meets formal standards and requirements for PPCs. Nevertheless, its effectiveness is difficult to measure. While the meetings are announced to be held monthly, they take place only sporadically. Although the resulting decisions and suggestions are submitted to state ministries, the real effect of the private sector's feedback is insignificant.

The recent establishment of a Small and Medium-Sized Enterprise Development Council of the Republic of Armenia by the Prime Minister (July 2011) holds great promise for improvement in the area of PPCs and is expected to yield tangible results and demonstrate effective operation, as its objective is to raise and discuss issues specific to the SME sector. The meetings are held quarterly and the first three meetings have already addressed several issues critical for SMEs. The council could benefit from better representation from the business sector and the establishing of communication channels between the business sector and the council.

Establishing a conducive operational environment

In recent years, Armenia has made significant progress in the areas of company registration and simplification of administrative procedures. Introduction of e-government services and adoption of the silence-is-consent principle are among the most important developments. However, additional efforts are needed to increase the geographical scope of these services.

Company registration

Recent reforms to company registration have resulted in significant improvements in the cost and efficiency of the registration process. Amendments to the Law on the State Registration of Legal Entities were passed on 21 December 2010, reducing the legal time limit for issuing a company registration certificate from five days to two days. In March 2011, the Ministry of Justice established the Business Entry one-stop-shop, allowing for registration of the company name with the state patent department, company registration with the state registrar, and registration with the tax authorities to be completed in the same location within three to seven calendar days. Substantial progress has also been made in reforming the notification and compliance phases. As a result, entrepreneurs are only required to spend eight days and undertake three administrative procedures to complete the overall registration process. The government has also introduced a website for company registration, allowing new start-ups and individual entrepreneurs to submit documentation and obtain a company registration certificate online.

Unfortunately, the improvements in company registration are mostly felt in the capital city and main urban areas. In regional areas of Armenia, the limited adoption and availability of the Internet is restricting the acceleration of the demand for online registration services. Furthermore, one-stop-shops are currently only available in the capital city, Yerevan, and entrepreneurs in other regions do not have access to these facilities. Extending the geographical scope of one-stop-shops is an effective way of stimulating enterprise creation in other regions of Armenia.

The silence-is-consent principle has been adopted for company registration and for obtaining general business licences. This positive change sends a clear signal to companies that procedures will be conducted within a reasonable timeframe, and will further reduce the administrative burden on SMEs.

Interaction with government services (e-government)

The government of Armenia has recently made significant progress in the development of online services that encourage SMEs to adopt electronic forms of communication, but more time is needed to assess its success. An online portal has been established, with links to the websites of various e-government services. Online filing of tax returns and social security contributions is available through the website of the State Revenue Committee. However, the system has only been available since July 2010 and as such does not have a solid track record of implementation. At present, electronic submission of tax returns is only obligatory for certain groups of taxpayers (banks, credit institutions, insurance companies, large companies, etc.) and is available to all taxpayers in a non-mandatory (voluntary) way. Starting from 1 January 2012, electronic submission of tax returns is obligatory for those taxpayers whose turnover the previous year exceeded AMD 58.35 million (approximately EUR 115 000).

In order to encourage higher usage rates of e-government services from SMEs, it is necessary to provide users with an interactive and user-friendly interface and to increase the sophistication of current software to allow for credit and debit compensation. In response to these needs, the government has approved a concept paper: On Formation of E-society in the Republic of Armenia (2010-12). The plan includes measures to design and develop a range of online government services, including e-pension and e-procurement systems. A pilot project for online filing of pension forms is already available on the website of the Ministry of Labour and Social Affairs.

For the purpose of streamlining online reporting of enterprise statistics, the Ministry of Economy and the Enterprise Incubator Foundation (EIF) have developed ICT Stat, an online registry of ICT companies with thorough and accurate statistical data allowing for effective industry analysis. The system will serve as a pilot project for the online reporting of enterprise statistics in other sectors and industries. In addition, automated transfer of data from government institutions to the National Statistical Service is also envisaged in the concept paper: On formation of E-society in the Republic of Armenia (2010-12).

In order to file tax returns online, companies can use an electronic signature, which was introduced with the adoption of the Law on Electronic Documents and Electronic Signature in 2004. The Ministry of Economy is working to further integrate electronic signature with other e-government services.

Some preliminary steps have been taken towards increasing communication between public institutions. In 2009, a number of government ministries and public institutions adopted Mulberry Groupware, a specialised workflow management system that allows for centralised storage of electronic documents. However, administrative blocks are preventing the software from being used to its full capacity. In addition to updating current systems to reflect the latest advances in technology, increased co-ordination between government bodies is needed to ensure that new ICT solutions are effective in reducing the administrative burden on SMEs.

Bankruptcy procedures and second chance

Laws and regulations on bankruptcy procedures are established through the Law on Bankruptcy of 2006, amended in 2007, as well as through other legislative documents, such as the Law on the Bankruptcy of Banks, Credit Organizations, Investment Companies, Managers of Investment Funds and Insurance Companies. The liquidation and bankruptcy of state-owned enterprises are regulated within the same legislative framework, which makes bankruptcy procedures more transparent in Armenia.

The law is mostly compliant with international standards and has been significantly improved through its 2007 amendment, particularly as regards commencement provisions and the provisions relating to creditors and re-organisation proceedings. Indeed, an assessment of the insolvency framework conditions conducted by the EBRD in 2009 concluded that compliance with international standards was of medium quality (EBRD, 2009). Nevertheless, there is still scope for improvement as regards avoidance of pre-bankruptcy transactions and provisions dealing with the assets of the estate.

Relatively efficient insolvency proceedings are also confirmed by the results of Armenia's performance in the World Bank's *Doing Business 2012* report. Armenia is the top performer among the EaP countries in all three categories measured: bankruptcy time is 1.9 years, costs incurred through proceedings are only 4% of the estate's value and the

recovery rate for creditors is 40.3 cents on the dollar (which nevertheless is still low compared to the OECD average of 69.1 cents on the dollar). Thus, local companies undergoing liquidation or bankruptcy as well as creditors can expect relatively efficient treatment which saves time and cost for all parties involved.

Regarding second chance treatment, there are no discriminatory provisions in Armenia which would restrict access of re-starters to business support schemes or to participation in public procurement tenders. Moreover, the public administration plays a supporting role for quicker debt settlement given that tax debts take lower priority over secured creditors. On the other hand, there are no pro-active measures to promote previously failed entrepreneurs in taking a fresh start which could be achieved, for example, through providing information on procedures, training or other campaigns.

Facilitating SME access to finance and developing the legal and business environment

Small and microlending programmes are available in the country through banks, specialised microfinance banks and other credit institutions. Other sources of financing such as leasing and private equity are small or underdeveloped. The legal and regulatory framework has improved over the past few years, particularly regarding cadastre and credit information services, although additional efforts are needed to improve the enforcement of creditors' rights. Low financial literacy and a lack of transparency continue to affect SMEs' access to finance.

Sources of external finance for SMEs

The performance of the banking system has improved in recent years, following the implementation by the Central Bank of Armenia (CBA) of measures aimed at consolidating the sector, strengthening supervision, introducing new corporate governance regulations and enforcing penalties for non-compliance with prudential norms. Nevertheless, the banking sector is small, fragmented, and the range of financial instruments offered to enterprises remains limited. Bank lending and portfolio quality have been significantly affected by the crisis. While credit growth has recently picked up from less than 15% in 2009 to 27% in 2010, bank intermediation remains relatively low, with domestic credit accounting for about 33% of GDP at the end of 2011. Moreover, SME lending accounts for only an estimated 25% of domestic credit to the private sector, and access to finance is particularly restricted for SMEs in rural areas. Low financial transparency of SMEs, particularly in the agricultural sector, has led to universal mistrust of banks in financial statements, even if properly audited. This is why banks tend to rely heavily on collateral and would rarely consider a client with weak collateral coverage such as companies in rural areas. Lack of legislation has prevented the development of specific financial products such as trade finance and factoring.

The SME DNC Fund of Armenia provides credit guarantees to SMEs. Priority under the SME DNC framework is given to companies in the manufacturing, trade and services sectors operating in economically disadvantaged areas. The framework also supports companies operating in production aimed at import substitution or exports and those devoted to innovation and new technologies. The guarantees provided by the SME DNC cover up to 70% of the total debt for a maximum of three years, and are capped at AMD 15 million (USD 39 000). Since 2004, the aggregate amount in guarantees granted by the SME DNC has been estimated at around AMD 1.5 billion.

In addition, in 2006, under the SME DNC framework of the Start-up business support programmes, the United Nations Development Programme (UNDP) for Armenia established a revolving fund to provide financial support for start-up entrepreneurs and to improve their credit terms. Within this framework, loans up to AMD 3 million (USD 8 100), fully guaranteed by SME DNC, are provided to start-up entrepreneurs through partner banks based on an assessment of their proposed business plans. Currently the amount of the revolving fund is approximately USD 400 000.

Microfinance institutions are an important source of finance for SMEs in the region. The sector is regulated by the CBA. There are over 25 universal credit unions operating in the country, mainly privately funded, as well as a microfinance bank (Procredit Bank). These are the main providers of microfinancing. The largest microfinance institutions have a wide outreach throughout the whole country with branches in nearly every region. Financial services for specific groups exist although their scope is very limited.

Leasing is developing as an alternative source of financing for SMEs. The legal framework for leasing activities is defined by the Civil Code and the Law on Credit Organizations. A specific law on leasing activities is currently under consideration. The CBA regulates this sector as part of the financial market. There are only a few leasing companies operating in Armenia (including ACBA leasing, Unileasing and Agroleasing) and the scale of leasing operations is relatively small. In 2010, the volume of leasing activities in Armenia was USD 27 million representing 0.3% of GDP.

A commercial private equity sector is yet to develop and, so far, the country has attracted very limited interest from international investors. A number of international financial institutions (EBRD, IFC, BSTDB and FMO) have jointly provided financing to the first equity fund specifically dedicated to the Caucasus region. Legislation relating to risk capital has been in place since January 2011 when the Law on Investment Funds came into force. However, the business environment continues to be difficult, investment opportunities and exit possibilities are limited, all contributing to the lack of development of private equity finance.

Securities market legislation is well developed with the Law on Securities Market Regulation enacted in 2007, but it remains weakly enforced. The Armenian Stock Exchange, established in 2000, was acquired by Nordic stock exchange operator (NASDAQ OMX). NASDAQ OMX Armenia has various levels of requirements applicable to companies and securities included in different stock exchange lists (main and secondary lists for stocks and bonds), which allow SMEs to choose the appropriate listing. However, the equity market remains small and illiquid with market capitalisation and turnover around 1.5% of GDP and 2% of GDP respectively as of the end of 2010.

Legal and regulatory environment

The real estate cadastre system is fully functioning and its database is connected to the Mulberry system of management of electronic documentation (Armenia is ranked fifth in property registration by the World Bank's *Doing Business 2012* report). However, online cadastre services are not available yet, although the necessary infrastructure is currently being set up. Accepting real estate as loan collateral is a widespread practice amongst creditors in Armenia although certain limitations remain in rural areas. The lack of a transparent online system of registration of real estate transactions affects banks' ability to obtain information on the value of collateral, particularly for rural areas.

The credit information system is well developed and includes both private and public credit registries. ACRA Credit Reporting CJSC, the private credit bureau, has been operating in Armenia since 2004. The bureau provides credit information services to all financial institutions and holds historical data for a period of five years. Borrowers may obtain their personal data held by the credit bureau upon request. The information provided is comprehensive and regularly updated. Efforts are also being made to collect and distribute information from utility companies. The Armenian public credit register has been operated by the CBA since 2003 for regulatory purposes. The information is available to financial institutions and to the public upon request. However no more than two years of data are kept on the public registry. The registry covers 23.7% of adults, reflecting the low outreach of financial services in Armenia.

A system of state registration of leasing rights and pledges on movable property was introduced in 2004. The registry functions are carried out by the State Committee of Real Property Cadastre which is the body originally entrusted with the real estate property cadastre. The registration procedure requires the filling of the full security agreement and the law sets exhaustive lists of additional documents needed for registration as well as of reasons for rejecting it. However, although a single database for movable property registration was created by law, it lacks effectiveness because it is not an electronic registration and the information is accessible only upon submission of a written request. In addition, the information it contains is limited in scope and the registration of pledge is not mandatory except when a specific statute prescribes so for a certain type of asset.

Although the CBA does not enforce direct rules on collateral or provisioning requirements, regulations regarding high reserve requirements (uncollateralised or "blank" loans) may indirectly lead to stringent requirements with respect to the collateral required by commercial banks. Nevertheless, SMEs and recipients of group (community) loans benefit from flexible collateral requirements which are applicable to microlending. A number of banks and other credit organisations provide loans without collateral and require repayment guarantees instead.

Armenia's Law on Bankruptcy stipulates that the assets of the borrower filing for re-organisation are frozen, preventing the creditors from seizing assets held as collateral. The creditor's consent is not required before an entity files for re-organisation. However, secured creditors have priority on the proceeds from the sale of collateral during liquidation. Directors of the company filing for re-organisation are prevented from exercising their management rights until the end of the re-organisation process.

Other factors that affect demand and supply of finance

Awareness of financial services is quite low. This is demonstrated by the low proportion of adults holding an account in commercial banks (163.7 accounts in commercial banks per 1 000 adults – much lower than in OECD countries). However, since 2008 significant efforts have been made to increase the financial literacy and awareness of the population. For example, the Union of Banks of Armenia has recently launched a financial e-library (with financial support from USAID) which includes a large number of written documents on different aspects of banking and finance. Taking into consideration OECD's principles on financial education, in 2009 the CBA prepared a three-year programme on The improvement of economic and financial literacy in the Republic of Armenia.

Promoting a culture of entrepreneurship and skills development

The importance of entrepreneurship for the country's sustainable economic growth and national competitiveness is now fully recognised and the promotion of entrepreneurship and SME development programmes are increasingly supported by the government.

The government still needs to improve institutional conditions for developing an entrepreneurial society and for the promotion of an entrepreneurial mindset. The first steps in establishing policy partnerships between the government, social partners and the education system have been made to increase the effectiveness of vocational education and training (VET) in the country and to align the supply of skills more closely with the needs of the economy. Social partners have contributed to the adoption of the Concept of the Social Partnership in initial vocational and secondary specialised education, and the memorandum of understanding (MoU) for co-operation in initial and secondary professional education has been signed between the Ministry of Education and Science (MES), the Republican Union of Employers of Armenia and the Chamber of Commerce and Industry.

There are elements of lifelong entrepreneurial learning (LL EL) in the education curricula: in 2010, a mandatory subject, social science, was introduced in education programmes. It includes elements of economics, psychology, ethics and safety. This subject covers entrepreneurship skills development and is taught in 100 (out of 107) schools in Armenia, as part of the 10th grade curriculum. The MES actively co-operates with the programme Junior Achievement of Armenia to support the introduction of elements of entrepreneurship into school education, teacher development and projects focusing on the economic literacy of young people. There are also adult learning support programmes jointly with DVV International, a German development agency, which contribute to the overall entrepreneurial learning support in the country.

There are no systematic statistical data on non-formal learning at the national level. Around 200 service providers offer various courses from language to computer training. Entrepreneurial learning has not yet become a substantive part of non-formal learning, and the training market itself is quite fragmented. A series of TV programmes disseminate results of the activities of SMEs (SME DNC) on a weekly basis, cover training support programmes in the regions and business services provider updates, relate SME success stories, etc. These video materials can be found on the SME DNC website.

Armenia is gradually creating an enabling policy environment and a regulatory framework for SME development, and is building a training and support framework for newly-established and growing enterprises through the adoption of the Concept for SME Development Policy and Strategy, approval of the Programme for State Support to SMEs, implementation of training courses for SMEs by business training providers and through specialised courses responding to the demands of enterprises.

The SME DNC, with state funding, provides services to SMEs, including business consulting and training, financial support, information support, etc. There is an online register of training providers and training programmes broken down by regions, and reference materials for SMEs are accessible on the web. The centre conducts training and mentoring services for both start-ups and ongoing businesses. In 2009-10 around 20 000 new companies were registered in Armenia, of which 5 000 companies received services through SME DNC. SMEs in Armenia also benefit from training services provided by the Chamber of Commerce and Industry, the Business Support Center, the Union of Information Technology

Enterprises, the Enterprise Incubator Foundation and other providers. The State Employment Service Agency of the Ministry of Labour and Social Affairs offers training programmes to the unemployed and disabled, some of which are dedicated to preparing individuals for future self-employment. More than 20% of the 4 578 persons involved in the programme in 2008 and 2010 have actually started their own businesses. Though a systemic training needs analysis (TNA) framework has not yet been established at the country level, a regular training needs analysis is being implemented by the SME DNC through surveys among SMEs, and by evaluating the outcomes of such state business support programmes. TNA is carried out by other training providers, employer organisations and projects for SME support on an *ad hoc* basis, *e.g.* a joint committee (government, major ICT companies, enterprises and social partners) analyses the training needs of ICT sector enterprises.

Out of the 130 000 companies registered in Armenia, about 700 are owned by women. The Gender Policy Concept Paper was approved by the government in 2010. Both the concept and the Gender Policy Implementation Strategy reinforce an increase in the role of women in entrepreneurship development as a main objective of gender policy in Armenia. There are presently no measures for direct support of women's active participation in business activities or for stimulating their self-employment being implemented by the state.

Armenia aims at promoting quality assurance in both formal education and business training for SMEs. A National Centre for Quality Assurance of Tertiary Education Foundation has been supporting quality assurance in universities, vocational and training schools since 2008. The draft Guiding Principles for Tertiary Level Educational Establishments on External Quality Assurance have been recently developed. The Centre for Education Projects of the MES implements projects for the improvement of education quality and its relevance. The National VET Council – as a tripartite body – guides vocational education and training sector reform and the overall improvement of the quality and relevance of VET. There is no national quality assurance framework of training programmes for SMEs, but *ad hoc* measures are being implemented, such as using quality monitoring tools by training providers and assessment of the outcomes of training courses for small enterprises. Accreditation of business training providers has not yet been introduced in Armenia.

In 2009-10, the Start-up business support programme provided training and mentoring services for 325 entrepreneurs at the stage of business start-up in the regions of Armenia. During this period, 100 new small enterprises received state registration and launched their business activity. This state-supported start-up training gives preference to entrepreneurs from the bordering and distant regions.

Development of knowledge and skills for enterprise growth is a priority in the national economic development plan and is supported by the business community. The government provides financing through annual programmes of support to SMEs for training and advisory services to active businesses to stimulate their enterprise growth. Although state resources are limited and do not cover all the needs for enterprise growth, they ensure the implementation of a critical element of the national growth strategy. Further development of training and a support system for start-ups and growing enterprises requires the systematic collection of data, as well as analysis of the impact of programmes. This is critical to the improvement of skills of human capital in Armenia.

Enhancing SME competitiveness

Armenia has shown full commitment to developing the appropriate tools to improve the competitiveness of SMEs, starting from the provision of basic informational and business services to start-ups, to innovation support schemes to technological firms. Adoption of a strategic approach to improve the competitiveness of SMEs, as well as further co-ordination of existing programmes can significantly improve the effectiveness of SMEs.

Business information and services

The main actor in providing business, technical and financial services to SMEs in Armenia is the SME DNC Fund, which functions within the framework of the annually approved state action plan. The services provided include: start-up support, product promotion and branding, export support, introduction of new technologies, provision of business information, consulting and training support through the Enterprise Europe Network (EEN), as well as financial assistance. The fund has wide geographical coverage via its 10 regional offices, and focuses on rural and peripheral areas. Out of the total number of enterprises served at the SME DNC, only 21.2% are from Yerevan. The roll out of technological advancements beyond the capital, especially to foster e-platforms for information services, could further facilitate the interaction with the SMEs in different locations.

Other development agencies and support units that provide information support and advisory services are the Armenian Development Agency (ADA), the Union of Manufacturers and Businessmen of Armenia, the Chamber of Commerce of Armenia and other private sector associations. Private business services providers (BSPs) in Armenia are also quite active in providing consultancy and other support services to SMEs, but these services are usually limited to accounting, audit and business consultancy. Due to their profit orientation, specialised and customised services for SMEs and business start-ups are generally insufficient.

As already mentioned, the SME DNC Fund provides a Start-up Business Support programme in collaboration with UNDP Armenia. The programme provides full-cycle support to local SMEs, which combines two-month training, consultations on developing business ideas, drafting a feasible business plan, support in implementation and financing, etc. At the end of the process financing is provided based on the approval of the business plan by an expert team. In 2011, the budget of the programme was USD 320 000 (approximately EUR 240 000), with 60% funded by the state.

Start-up support is complemented by the Enterprise Incubator Foundation (EIF), one of the largest business development and incubation agencies in the region. Established in 2002, it provides various advisory and business services, as well as office facilities. The agency mainly targets start-ups in the area of information and communication technology (for more details, see Innovation below).

Public procurement

Public procurement is regulated by the Law on Procurement, which came into force on 1 January 2011. Armenia strives to ensure competitive public tendering with standards that are aligned with EU practices. The government treats tenders from national and foreign operators equally.

The procedures likely to facilitate the access of SMEs to procurement include:

- Cutting tenders into lots, where the law prohibits combining procurement subjects with different descriptions into one lot, if they can be presented in separate lots.
- The possibility to present joint tenders, where the law prescribes taking into account the unified qualifications of all parties of a joint venture/consortium.
- The qualification and financial requirements are defined by the needs of the contracts, although there is no indication of practices on the ground.
- Finally, according to government sources, typically late payments by public authorities do not present a significant problem in Armenia. However, this information is not supported by any statistics.

Armenia centralises all tender invitations at the national level to ensure more transparency for economic operators. Information is disseminated via a dedicated website: the Public Procurement of the Ministry of Finance of the Republic of Armenia (*www.gnumner.am*), which is currently limited to the provision of basic information regarding tenders. Announcements on TV and radio are also used, but no further information is provided on how this works in practice. Ministries are working to put into place the necessary ICT framework for e-procurement. Training is conducted by the Ministry of Finance for co-ordinators of procurement.

Innovation policy

The Concept of Jump-start Strategy for Designing Innovation Economy, approved in 2011 by the Ministry of Economy, provides a clear vision for increasing the competitiveness of the national economy via innovation and specialisation in specific sectors of the economy. The document is a comprehensive plan for the development of innovation policy in Armenia. It identifies all major innovation support programmes (both projected and underway) and includes a strategic vision to 2020 for the formation of a national innovation system.

There are various private and donor-funded innovation and technology centres in Armenia. For instance, the Microsoft Innovation Centre provides local IT communities with programmes and services to expand work-force skills, create jobs and strengthen and improve competitiveness. In addition, the government of Armenia has developed and approved an action plan for the establishment of a large-scale technology centre in the north western city of Gyumri. The centre will provide technology support and incubation services to local firms and entrepreneurs.

Financial and technical support schemes for innovative companies are provided on an *ad hoc* basis, and are largely directed towards high-tech companies. Both the EIF and SME DNC provide specialised financial support for innovative start-ups. However, the availability of non-technological innovation support schemes (*e.g.* business planning, consultancy services) for SMEs is very limited.

Despite a common concept, the Armenian innovation policy is still fragmented in several strategic papers, and various innovation initiatives are not co-ordinated at the national level. A dedicated government institution or co-ordination body would allow for further integration of technological and non-technological innovation support services, and increased co-operation on innovation policy between government, industry and universities and research centres.

Green economy

Even though information regarding environmental issues as well as expertise and support in specific areas is available in Armenia, environmental issues are not addressed in the SME strategy. However, elements of greening of the economy are planned for inclusion in new policy documents in the future. Information regarding environmental issues as well as expertise and support in specific areas is available in Armenia.

There have been several sporadic initiatives and information events on environmental management standards (EMS) and several organisations are certified with ISO 14001 standards. However, there are no specialised programmes or policy support measures for raising awareness of environmental issues or for encouraging the business community towards these systems.

Export promotion

Given Armenia's small domestic market, Armenian businesses rely heavily on exports in order to expand. In its new Export-led Industrial Strategy adopted in 2011, the government of Armenia is dedicated to promoting export capacity of national businesses, to strengthening policies for export promotion and to the synchronisation of national regulations and laws with EU standards.

Currently, SME export promotion activities are provided by the SME DNC Fund, within the framework of the Annual State Support Program for SME Support and by the ADA. Both provide quality information, guidebooks for exporters, specialised advice and assistance with regard to exporting procedures, training in promotion of Armenian products in foreign markets, as well as financial support by covering the full or partial costs of participation of firms in international trade fairs. As a member of the EEN since 2008, the SME DNC Fund offers information on EU certification procedures, lists organisations providing certificates and describes customs procedures related to export to the EU market (see single Market opportunities below). The ADA performs a liaison role with potential investors and exporters and is also conducting extensive analysis of potential target markets, such as those in the Middle East.

The Export-led Industrial Strategy of Armenia, in force as of 2012, aims to promote the exports in a strategic approach in prioritised sectors based on public-private partnership mechanisms. Even though the focus of interventions differs from sector to sector, general areas addressed in the strategy are: quality assurance, technology transfer, workforce development, access to external markets and innovation.

The new strategy for SME development establishes links between the Export-led Industrial Strategy of Armenia and SME issues for SME development. In order to gain maximum efficiency from state interventions, the Export-led Industrial Strategy could be synchronised with SME policy. The export promotion schemes could then be tested on selected sectors with a specific focus on encouraging SMEs to export their products and services.

Single Market opportunities

In view of the start of negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA), to be held in 2012, Armenia has made substantial progress on legislative and institutional reforms in the areas of technical barriers to trade and sanitary and phytosanitary rules.

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To address technical barriers to trade, the Armenian government has prepared four fundamental laws on technical regulations, standardisation, accreditation and uniformity of measurements. In addition, a government programme of alignment with the EU legislation has been drafted, identifying priority sectors with a special emphasis on those which are most economically significant.

To address sanitary and phytosanitary rules, in 2011 Armenia adopted a food safety strategy and a related action plan aiming at gradual approximation with EU standards. Legislation on food hygiene and inspections was also adopted. A risk assessment centre was established and a network of state laboratories trained staff with EU support.

SMEs are informed by the SME DNC, the ADA, the EEN and the Chambers of Commerce on export conditions and opportunities for Armenian enterprises planning to engage with the EU.

The way forward

Based on the SBA assessment, Armenia could consider the following steps to ensure continuing progress in the area of SME development:

- The country would benefit from adopting a **strategy for SME development** (which is currently being developed) and continuing business environment reforms based on an inclusive public-private consultation mechanism in which SME interests are taken into account. The state allocations for SME support should be scaled up to ensure effective implementation of the strategy and a successful continuation of current programmes. The strategy should embrace human capital and entrepreneurship development issues among the policy measures supported under the SBA framework. It is also recommended to include elements of eco-efficient business and product innovation in the SME strategy.
- The **effectiveness of public-private consultations** could be enhanced by further strengthening the role of SME representatives in reactive and pro-active consultations. The newly established SME Support Council could be further developed into an effective platform for public-private dialogue to consult on critical issues that are still limiting SME development. The representation of SMEs in consultations should be ensured by promotion of consultations among the business sector and creation of accessible channels for the private sector to voice their concerns and deliver them to the council.
- Further improvement in the legal and regulatory framework is essential for **supporting access to finance for SMEs**. An effective functioning of the central collateral registry would affect the ability of SMEs to provide collateral and significantly improve their access to bank finance. Ensuring effective creditor rights to allow secured creditors to seize their collateral after re-organisation would also help to improve bank finance to SMEs. Promoting financial literacy and transparency of SMEs would positively affect their ability to obtain finance from banks. A competitive and more sophisticated banking sector will facilitate sustainable access to finance to SMEs. Further improvement in the business environment (to increase investment and exit prospects) would support growth of private equity capital.
- **Strengthening of export promotion schemes** for SMEs could be considered to further support SMEs in reaching export markets, given the small size of the domestic market with limited opportunities for business growth. Schemes to support export companies could be tested first in relevant priority sectors of the economy with export potential.

The export-led industrial strategy could also be synchronised with a sectoral approach and horizontal SME development initiatives in order to gain maximum efficiencies from state interventions. Armenia is invited to further improve its administrative and regulatory information for SMEs on Single Market issues.

- **Innovation policy** is another key area to be addressed. Though there are notable improvements and there is commitment to the development of innovation, the non-technological sector still lacks dedicated policy, resources and mechanisms for fostering innovative activities. Specific tools and mechanisms for fostering innovation could be developed, such as matchmaking grant schemes for promoting co-operation between university/research institutes and private business and acquisition and adoption of modern technologies (technology transfer).
- Finally, the **availability and quality of statistical information** is one of the central requirements necessary for analysing and tracking the development of the SME sector. Data availability could be improved by conducting regular enterprise surveys of a statistically relevant group of SMEs covering all sectors of the economy and in all regions. It would be especially important to monitor and evaluate the performance of companies that have benefited from state support, *e.g.* through training, start-up support, grants, business services. Systematic collection of data would ensure better targeting of government support measures, analysis of the training needs of enterprises, monitoring of the non-formal learning provision in the country and evaluation of the impact of programmes, such as those for women entrepreneurs and youth.

Notes

1. Registered unemployed only; based on data from Armstat.
2. The data is originally taken from the Legal Entities State Registry Agency of the Ministry of Justice of the Republic of Armenia.
3. Unfortunately, at the time of writing this publication more recent data was not available.
4. The estimated figure does not include agriculture and net taxes.
5. Employees engaged in state governance and agriculture are not included.
6. These figures refer only to those companies that are included in regular monitoring by the National Statistical Service. The companies monitored do not include farmers who, according to national statistics, account for approximately 45% of employment. Even though SME DNC covers a more extensive pool of indicators, many of them being expert estimations, the frequency of the publications and the variety of information sources used for the calculations are scarce.
7. Subsistence farming, whose production output is exclusively for a household's own final consumption is implicitly accounted for in the formal sector.
8. This paper was adopted in 2000 and does not fully reflect the current situation of SMEs and national priorities; it is currently under review. The strategy paper is being elaborated by a group of experts with technical assistance provided by GIZ (Deutsche Gesellschaft für Internationale Zusammenarbeit GmbH).
9. The information provided by the National Statistical Services is based on a limited number of firms that are included in regular monitoring, which is biased towards large firms and covers only six sectors: manufacturing, services, transport, telecommunications, trade and construction.

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PART III

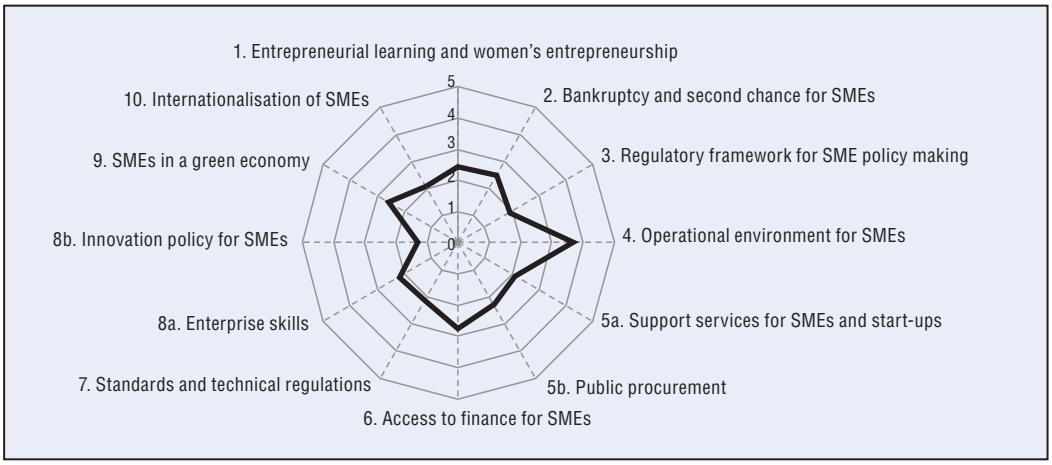
Chapter 14

SBA country profile: Azerbaijan*

In recent years, Azerbaijan has made significant progress in acknowledging the key role of small business in the diversification of its economy, and in setting up an institutional and legislative framework to address the issues of entrepreneurship. The Small Business Act (SBA) assessment identified the improvement of the regulatory environment as one of its main achievements. There has also been progress in simplification of regulation by reducing the number of days, procedures and costs required to start a business, as well as the introduction of online registration for both individual entrepreneurs and legal entities. Nonetheless, much remains to be done in strengthening horizontal intra-governmental co-ordination mechanisms and creating more opportunities for the small business sector to be involved in the policy-making process through public-private dialogue and its better representation within associations and other advocacy groups.

* This chapter was prepared with the support of the Azerbaijan Marketing Society and Alakbar Mammadov.

Figure 14.1. **SBA scores for Azerbaijan**



Note: The scores for each dimension are calculated based on assigned weights for each indicator (see Annex A for further information).

Overview

This section provides a brief economic snapshot and highlights some recent trends in the business environment. This is followed by a detailed overview of the current situation of the SME sector in Azerbaijan.

Economic snapshot

During 2007-09, the GDP of Azerbaijan grew on average by 15%. As oil production reached a peak, GDP growth was 5% in 2010 and it slowed down to 0.1% in 2011 (EBRD, 2011). According to the State Statistical Committee of the Republic of Azerbaijan, in 2011, oil and oil-related activities accounted for 51.7% of GDP and 92.3% of exports. The reliance of the economy on oil exports represented a buffer against the financial crisis, allowing a GDP growth of 10% over 2008-09. In 2011 the growth has declined due to a decline in oil production. Nevertheless, during the same year, the non-oil sector grew by 9.4%.

The main challenge for the country remains the diversification of its economy away from the oil sector. Significant benefits were derived from the boom in oil revenues after 1994. With the help of the State Oil Fund of Azerbaijan (SOFAZ) a large part of the revenues were invested in grand infrastructure projects and social transfer programmes. However, as the forecasts for oil production are now more pessimistic, the country could ensure its future sustainable development by encouraging entrepreneurial activity in order to create more businesses and jobs in the non-oil related sectors.

Business environment trends

In recent years Azerbaijan has embarked on a number of reforms, improving the business environment and increasing the attractiveness of the country for foreign investors. The main improvements were carried out in areas covered by the World Bank's *Doing Business* report. The country was named the region's main reformer in 2007-08, with positive changes in seven out of the ten *Doing Business Indicators*. In 2007-08, the country made reforms in seven out of the ten indicators and was named the main reformer among 181 countries (World Bank, 2008). With the support of the Azerbaijan Corporate Governance Project, run by the International Finance Corporation (IFC), corporate governance in Azerbaijan has

Table 14.1. **Azerbaijan: Main macroeconomic indicators, 2008-12**

Indicator	Unit of measurement	2008	2009	2010	2011	2012 (proj.)
GDP growth	Per cent, y-o-y	10.8	9.3	5	0.1	3.5
CPI inflation	Per cent, average	20.8	1.5	5.7	8.5	3.5
Government balance	Per cent of GDP	20	6.8	14.3	13.3	11
Current account balance	Per cent of GDP	33.7	23	28.4	26.5	22
Net FDI	USD million	–541	147	113	87	–220
External debt	Per cent of GDP	6.5	7.9	7.5	7.7	8.3
Gross reserves	Per cent of GDP	13.9	12.5	12.4	16.7	16
Nominal GDP	USD billion	48.9	44.3	52.9	64.8	72.2

Note: Data for gross reserves provided by the national sources is significantly different from those provided by IMF. The table shows the IMF data.
Source: 2011 (data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks).

significantly improved, with a jump from 96th to 33rd position. This has led to increased investment in the country. In 2010-11 a number of reforms were undertaken to improve the judicial system and reduce corruption (EBRD, 2011). The authorities also continue to participate in the Extractive Industries Transparency Initiative (EITI).

Despite improvements in the business environment and a good legislative framework, corruption is perceived to be very high. According to Transparency International, Azerbaijan ranks 143rd in the Corruption Perception Index 2011.[1] Independence and transparency of the judiciary are also factors hindering business development and growth (USAID, n.d.).

SMEs in Azerbaijan

According to data provided by the State Statistical Committee of the Republic of Azerbaijan, in 2011 there were 364 581 registered individual enterprises and 60 223 registered small enterprises. Among these only 185 050 individual entrepreneurs and 38 336 small enterprises were active, representing 94.4% of the total of active entities in 2011 (83.1% and 11.3% respectively). The numbers are based on the definition approved in 2009: all individual entrepreneurs are legally considered to be small enterprises, whereas those registered as legal entities are classified according to the approved definition (see Table 14.2).[2]

Table 14.2. **Definition of small entrepreneurship in Azerbaijan**

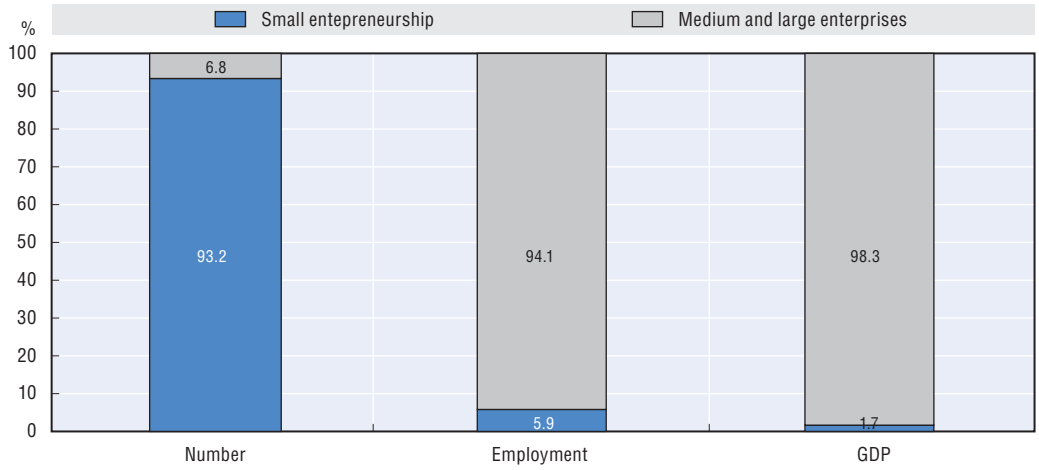
Economic activity	Employment	Turnover
Industry and construction	< 50	≤ AZM 500 thousand (EUR 454.5 thousand)
Agriculture	< 25	≤ AZM 250 thousand (EUR 227.3 thousand)
Wholesale trade	< 15	≤ AZM 1 million (EUR 900.9 thousand)
Retail trade, transportation, service and other economic activities	< 10	≤ AZM 250 thousand (EUR 227.3 thousand)

Source: Decision of the Cabinet of Ministers of the Republic of Azerbaijan, 18 December 2009.

Most small enterprises are operating in low-value added sectors. According to the Statistical Committee of the Republic of Azerbaijan, in 2011 a significant proportion of small enterprises (excluding individual entrepreneurs) were active in wholesale and retail trade (32.5%),[3] agriculture, forestry and fisheries (15.2%), construction (13%) and manufacturing (7.9%). The majority of individual entrepreneurs were involved in trade, transport, services and agriculture.

In 2011, more than half of the newly-established enterprises (61.5%) were registered in Baku, 10.3% were registered in Aran, 7.6% in Absheron, and 5.3% in Ganja-Gazakh, revealing significant regional disparities in business activities. Most individual enterprises were registered in Baku as well.

Figure 14.2. **SME sector in Azerbaijan, 2010**



Note: Based on active enterprises; data on employment and GDP do not include individual entrepreneurs.
Source: State Statistical Committee and Ministry of Economic Development.

SBA assessment results

This section outlines the main results for the Republic of Azerbaijan from the 2012 SBA policy assessment of Eastern Partner (EaP) countries. The assessed policy dimensions reassembled and grouped under five wider SME policy areas.

Strengthening institutional and mechanisms for SME policy making

Since 1999, the importance of small entrepreneurship and the need for support for the sector has been acknowledged through reforms aiming to regulate and support small business.

Institutional framework

In 1999, Azerbaijan adopted a number of legislative acts aimed at regulating the development of small entrepreneurship. The Law on Support to Small Entrepreneurship envisages areas of state support for entrepreneurship, such as development of infrastructure, development and implementation of support programmes for small entrepreneurship, ensuring preferential conditions for small entrepreneurship when obtaining financial, material, informational, scientific and technical resources, support in training and retraining of employees, etc. The law also defines criteria for small entrepreneurship that can enable them to benefit from state support.

Development of entrepreneurship constitutes one of the priorities of state policy aimed at diversification of the national economy. Currently Azerbaijan does not have a strategy for SME development *per se*, but elements of entrepreneurship support and specific measures have been included in the wider national State Program on Social-Economic Development of Regions of the Republic of Azerbaijan (2009-13), the State Program on Poverty Reduction and Sustainable Development in the Republic of Azerbaijan (2008-15) and in the associated action plans.

The Ministry of Economic Development of the Republic of Azerbaijan is the institution responsible for the development and implementation of policy for the support of small entrepreneurship, and, more generally, has the mission to create a more favourable environment for business development. There is no one agency responsible for SME policy implementation. However, three agencies in the Ministry of Economic Development – the Azerbaijan National Fund for Entrepreneurship Support (providing financial support), the Baku Business Training Centre (providing consulting and training services) and the Azerbaijan Export and Investment Foundation (providing support for finding investors and export activities) – provide support to businesses within the framework of state policy. Another vehicle supporting the development of SMEs in Azerbaijan is the Azerbaijan Investment Company, which supports the development of the non-oil sector of the economy via termed equity injection along with local and foreign co-investors into the greenfield and brownfield projects in Azerbaijan.

Moreover, few statistical data are available on the size and performance of the SME sector. General information is available at the Ministry of Economic Development and the State Statistical Committee, but it is limited to basic data such as number of firms, GDP and employment. Collecting qualitative and detailed data about the SME sector could significantly improve the ability of the public authorities to analyse the sector and adopt relevant support measures.

Legislative simplification and regulatory impact analysis (RIA)

The Ministry of Economic Development reviews business-related legislation on an *ad hoc* basis, through its activities with the World Bank's International Finance Corporation (IFC). The review and simplification of legislation takes place in key priority areas designated by the World Bank's *Doing Business* report, such as starting a business, dealing with construction permits, obtaining credit and other indicators. A more comprehensive approach would require the development of a national regulatory reform strategy and the appointment of key institutions to review the existing stock of laws and regulations.

In Azerbaijan there is currently no legal framework in place for RIA and the SME test. In order to keep the regulatory environment free from becoming overburdened, newly introduced laws and regulations should be subject to a comprehensive impact assessment, and a formal evaluation of potential impacts on the SME community should be carried out.

Public-private consultations (PPC)

Despite several attempts to institutionalise the relationship between the government and business, public-private dialogue in Azerbaijan could be further strengthened. The Entrepreneurship Council under the President of the Republic of Azerbaijan was created in 2002.[4] Its main purpose is to promote the development of entrepreneurship and, in this regard, to prepare suggestions to the President of the Republic of Azerbaijan.

In 2001, the Cabinet of Ministers of the Azerbaijan Republic, Azerbaijan Trade Unions Confederation and the National Confederation of Entrepreneurs (Employers) of the Azerbaijan Republic signed the Trilateral General Collective Agreement, which stipulates co-operation between the organisations in the areas of social and economic situation in the society, minimisation of social disparity and promotion of living standards of the population. As well, it identifies obligations of the partners to develop mutual co-operation on the basis of social partnership principles and collective bargaining agreements and contracts. Furthermore, the National Confederation of Entrepreneurs (Employers) of the Republic of Azerbaijan has a

partnership agreement with Ministry of Economic Development, Ministry of Finance and other ministries and organisations. Established in 2002, it formally represents the interests of the business community. Annual events, chaired by the President of the Republic of Azerbaijan, are organised with the participation of ministries and other government institutions, as well as entrepreneurs. In addition, annual meetings are carried out to discuss the state programme "Socio-Economic Development of the Regions of the Azerbaijan Republic in 2009-13", where representatives of both private and public sector participate.

Overall, the role of domestic private businesses and civil society as agents of economic change remains modest in Azerbaijan. Small businesses have little influence and make little contribution to policy making. Despite the abovementioned consultation bodies there are no strong associations or groups representing small businesses that could be actively involved in a policy debate, move forward the interests of small firms and provide feedback on new and existing legislation. As part of the general business culture in Azerbaijan, businesses prefer to deal with their issues individually, rather than delegating the task to representative bodies, which do not have much formal influence.

Establishing a conducive operational environment

Azerbaijan has done significan reforms in the operational environment for businesses by streamlining company registration and establishing e-government services.

Company registration

Reforms to the company registration process have been highly effective in reducing the administrative burden for entrepreneurs and SMEs in Azerbaijan. In particular, the introduction of one-stop-shops under the Ministry of Taxes has significantly reduced the time and cost of registration. As such, according to World Bank's *Doing Business 2012* report, entrepreneurs are required to spend just eight days and undertake six administrative procedures to register a business in Azerbaijan. In addition, the state fee for registration has been reduced to AZM 11 (approximately EUR 10), and all other related costs (notary fees, bank charges, etc.) amount to AZM 120 (approximately EUR 115).

Substantial progress has also been made in shifting the burden of notification from the entrepreneur to the public administration, with no official requirements for entrepreneurs to register separately with other administrative authorities. However, one-stop-shops do not currently allow for all registration procedures to be completed at one window. Further reforms should aim to reduce or simplify a number of compulsory pre-incorporation procedures, including the need to obtain a lease agreement to confirm the legal address of the company's permanent governing body.

The Ministry of Taxes has recently made efforts to further increase the accessibility of registration services. In February 2012, it introduced online registration facilities for limited liability companies with domestically raised equity, removing the requirement to notarise documents when registering online. However, the system does not have a solid track record of implementation, and it is not clear whether all stages of the registration process can be completed online.

The silence-is-consent principle has not been introduced to business-related legislation in Azerbaijan. Implementation of the silence-is-consent principle for company registration would reduce delays in the application reviewing process, increase transparency and reduce opportunities for discretionary and informal settlements. These measures were recommended in a study of SMEs in Azerbaijan, published by the World Bank IFC in 2009.

Interaction with government services (e-government)

Electronic filing of tax returns has been available in Azerbaijan since 2006 through the Ministry of Taxes. Online submission of tax returns and online exchanges of tax-related information has led to reduced administrative costs for both the government and the private sector.

The provision of a wide range of e-government services is essential to lower costs, increase transparency and make public services more accessible to SMEs. There is currently considerable scope to develop e-government services in Azerbaijan, allowing for online filing of social security contributions, online reporting of enterprise statistics and online access to pensions, procurement and cadastre. The government is currently working to increase the range of online services available to entrepreneurs under the action plan of the State Program on Development of Communications and Information Technologies in the Republic of Azerbaijan in 2010-12 (E-Azerbaijan). The Ministry of Communication and Information Technology is also in the process of establishing a specialised state agency in charge of e-government, and additional online services such as an online cadastre registry are expected to be introduced by the end of 2012.

Azerbaijan has taken positive steps to further develop infrastructure for e-government. In particular, the recent introduction of an electronic signature system and the establishment of an operational accreditation body (National Certification Services Centre) is a positive step towards enabling direct interaction between SMEs and the government. In addition, developing links and sharing information between the databases of various public administrations can also significantly save time and reduce costs for SMEs.

Bankruptcy procedures and second chance

Bankruptcy and insolvency in Azerbaijan are governed by the Insolvency and Bankruptcy Law 1997 and the Civil Procedure Code 1999. The Insolvency Law scored "low compliance" when compared with international standards in the EBRD's 2009 Insolvency Sector Assessment project.[5] The Insolvency Law is deficient in most areas, with the exception of the treatment of creditors since it allows creditors to participate in insolvency proceedings and treats the claims of creditors in each class on an equal basis. Creditors also have adequate opportunity to seek redress from the court on matters with which they disagree.

However, general weaknesses of insolvency proceedings undermine these advantages. Especially problematic are provisions on the avoidance of suspicious pre-bankruptcy transactions, since they fail to provide the necessary details to create a predictable avoidance regime. The law also does not contain provisions requiring the registration or licensing of insolvency administrators, provisions on the appointment or review of insolvency administrators or on provisions on professional work standards, ethical rules or discipline for insolvency administrators.

In practice, the law has rarely been used since its adoption in 1997 due to the lack of trust in the judiciary system and a lack of knowledge on the part of stakeholders and main actors. As a result, Azerbaijan only ranks 95th (out of 183 economies) in the World Bank's *Doing Business 2012* Index in the indicator "resolving insolvency", which is lower than the EaP average (80).

Azerbaijan performs slightly better than the regional average on length of time for completion of bankruptcy proceedings (2.7 years against the EaP average of 3.2 years) and

bankruptcy cost (8% of the estate against the EaP average of 14.8%). The recovery rate (cents on dollars) is 29.7. It has gradually been falling over the last nine years from 33.4 in 2004. Discharge from bankruptcy for SMEs is not determined in the legislation. Public authorities could also play a more supporting role with regards to settling debt by treating tax debts as a lower priority.

Facilitating SME access to finance and developing the legal and business environment

Similarly to other countries in the region, bank finance is the main source of external finance for SMEs. However it remains scarce. Other sources of finance, such as leasing and microfinance, have recently increased in importance. The legal framework has particularly improved in terms of cadastre and credit registry. The implementation of a flexible definition of collateral, a registration system of pledge on movable assets and the enforcement of creditors' rights will contribute to the improvement of access to finance for SMEs.

Sources of external finance for SMEs

The low total amount of domestic credit available to the private sector, amounting to only 19.5% of GDP at the end of 2011, significantly restricts access to finance for SMEs. Although lending to SMEs has generally increased, the SME loan portfolio is estimated to account for only about 6% of total bank lending. The banking sector is largely locally owned and the state-owned International Bank of Azerbaijan continues to dominate the market with over 40% of market share. Although 44 banks operate in the sector, the banking system remains segmented and the top five hold 61% of total assets. Since 2005, the regulatory and supervisory framework has improved. The Central Bank of Azerbaijan has continued to seek sector consolidation through a gradual increase in capital requirements. Growth in credit to the private sector, while strong at more than 60% per year up to 2008 albeit from a low level, slowed substantially due to the crisis in 2009-10 (to about 9% in 2010). Non-performing loans have also increased considerably from 2008 reaching 6.4% in 2011. This has further affected bank lending to SMEs.

The leasing sector is under development. The Law on Leasing was adopted at the end of 1994. In 2003, the tax regime was made more favourable for leasing activities. Following favourable tax regime amendments in 2003, the country's leasing portfolio increased considerably. Increased competition in the sector has also resulted in the introduction of new products and services as well as some sectoral specialisation. According to the Azerbaijan Association of Leasing Companies, 44% of leasing companies operate in agriculture and 34% in construction. Nevertheless, important problems persist such as inadequate regulation that increases the costs of the leasing transaction for the lessee, the person to whom a lease is granted The total leasing portfolio accounted for only 0.25% of GDP in 2010, much less than the EU average.

Other sources of external finance for SMEs, such as risk capital and capital markets, are underdeveloped. The Law on Investment Funds was established in October 2010 and regulates risk capital. So far, there are two local investment companies present in the country; the state-owned Azerbaijan Investment Company and the Khazar International Investment Company. Venture capital is virtually non-existent. A difficult business environment and poor prospects restrict private equity activities. In Azerbaijan, the Baku Stock Exchange (BSE) has been operating as a trading and securities market since 2000. The

traded volume consists mainly of government treasury bills and bonds although equities and corporate bonds have increased since 2009. In 2010, the total market turnover represented 9% of GDP.

Public support to SMEs, mainly in the form of subsidised credit facilities, has been available since 2002 through the National Fund for Entrepreneurship Support (ANFES). This support is provided through local banks at a typically subsidised interest rate up to 6%. It offers small amounts of credit (AZM 5 000 to AZM 50 000), medium-sized credit (AZM 50 001 to AZM 500 000) and large credit (AZM 500 001 to AZM 1 million). Although the fund finances larger projects as well, the support system is designed to encourage the development of SMEs operating mainly in agriculture, industrial production, infrastructure and tourism across the country. In 2011, ANFES provided financial support to over 1 643 SMEs mainly in the agriculture sector, amounting to about AZM 138 million (USD 170 million). In addition, ANFES provides start-up funding for special groups such as young entrepreneurs and women.

Microfinance institutions are an important source of financing for SMEs in Azerbaijan. The sector has been regulated by the Central Bank of Azerbaijan since 2010. In 2009, the law was adjusted to permit microfinance institutions to collect deposits to ensure their long-term sustainability. As of August 2011, a number of microfinance organisations have been operating across the country servicing over 200 000 microborrowers. There are also 81 non-banking financial organisations providing microfinance, 12 of which are funded by international humanitarian organisations. According to the Microfinance Information eXchange (MIX), microlending accounted for about 2% of GDP in 2011.

Legal and regulatory environment

The cadastre of land and property is quite efficient because of the limited number of procedures and its low cost of registration. Time spent in the registration process has considerably decreased since 2008. Azerbaijan ranks 9th in property registration in the World Bank's *Doing Business 2012* Index. Even though land registration has considerably increased since 2009, land ownership has not been fully documented and online services are not available.

A Centralized Credit Registry (CCR), used by banks and credit institutions, was established by the Central Bank in 2005. Information concerning a person may only be released upon his/her consent. Debtors may access the registry and, for a fee, banks may consult it in order to assess potential clients. In February 2011, amendments and changes to the Law on Centralised Credit Register were adopted allowing organisations that provide loans (other than banks) to join the CCR. A project developed by the IFC is aimed at improving and implementing a legal framework for the sharing of credit information. It aims to increase the capacity and effectiveness of credit information bureaus and raise the public's awareness about the role of credit bureaus.

While there is no centralised collateral register of pledge on movable assets in Azerbaijan, mortgaged property is registered by the Real Estate State Register Service (ASRERS) after notarisation. Prior to accepting property as collateral, a bank requires documentation from ASRERS providing evidencing that the property in question is not pledged to another creditor. The legal position for taking mortgages (and for taking pledges) remains unclear as do the requirements and procedures for registration. Personal guarantee agreements in connection with small loans are concluded by the guarantors at

the relevant bank. Bank loans with principal amounts above AZM 5 000 (EUR 4 200) are subject to collateral, preferably real estate. Collateral levels remain high at around 200% of the loan amount.

The rights of creditors are protected by the Law on Pledge, adopted in 1998. This legal framework on secured transactions ensures the ability of secured creditors to seize collateral after re-organisation and the fact that secured creditors are paid first out of proceeds of the liquidation of a bankrupt firm. Management does not retain administration property pending the resolution of re-organisation. Further improvements are necessary to effectively enforce creditors' rights and ensure collateral recovery in case of bankruptcy.

Other factors that affect demand and supply of finance

There is no national strategy to promote financial literacy in Azerbaijan, although government awareness has recently increased. A special project related to financial literacy is also being prepared together with the Ministry of Education.

Promoting a culture of entrepreneurship and skills development

Azerbaijan is the only country in the region with a growing young population. Azerbaijan's oil industry still accounts for more than half of GDP, but does not generate much employment. Entrepreneurship is important in terms of employment and is essential for diversifying Azerbaijan's economy. Entrepreneurship is a widespread phenomenon in Azerbaijan and provides a future for many people.

There are many initiatives to support entrepreneurship including through education and training, many linked to each other. Many partnerships, sometimes as the result of formal policy processes and national programmes, encourage dialogue on entrepreneurship and entrepreneurial training issues. There are official steering committees for national programmes such as the National TVET Reform Programme, and the National Programme for Youth which include different public bodies, NGO's and employers and trade union representatives. The nature of such partnerships is rather formal.

More engaging and interactive co-operation can be found at the level of projects and donor activities that are based on informal and local arrangements or linked to a specific lead actor. Examples of these are the Adult Education Association, established in 2008, and the co-operation between vocational education and training schools and colleges and local entrepreneurs, or bilateral co-operation within the framework of EU-funded and bilateral education projects.

There is a clear need for defining roles and functions in entrepreneurial learning (EL) policy partnership, bringing together public and private stakeholders, encouraging the dialogue aiming at structured a lifelong EL policy framework – to reinforce common efforts. Although there are examples of initiatives by public and private partners as described above, there is no dedicated partnership mechanism for monitoring the development of entrepreneurial learning, for advising on policy improvement measures or for the exchange of good practice. Some existing institutional structures at the national level could consider bringing EL issues onto their agenda (*e.g.* the National Entrepreneurship Support Foundation, the Small and Medium Entrepreneurship Development Agency and Regional Entrepreneurship Centres).

Thanks to contributions from the Ministry of Education and the Committee of Women, Children and Families, the self-assessment for Dimension 1 on the policy framework for

entrepreneurial learning was completed. A positive development in the education system is that entrepreneurship, together with other core skills, is now integrated into a new national curriculum, introduced in 2007, for all general education students in Azerbaijan. The curriculum is being introduced gradually, and has so far only reached primary school pupils. Under the banner of life skills these pupils are introduced to entrepreneurship. For secondary school students the topic of life skills has become a compulsory extra-curricular part of the existing curriculum which is compulsory, but where students are not assessed. This initiative of the Ministry of Education is drawing on best practices in the Russian Federation and Kazakhstan.

Another example of good practice is an employer engagement manual that has been developed with the support of the British Council to assist schools in being more entrepreneurial in dealing with local companies. The Ministry of Education has also established an electronic network that provides information on courses, including entrepreneurship education for schools and for a wider public. With the support of the World Bank project Social Protection Development (approved in 2008), the State Employment Service is developing new working methods including active support to clients for establishing SMEs. Clients are trained on how to defend a business plan and how to obtain financial support. Information is available publicly on the web as well as through the distribution of brochures. The Baku Business Training Center has been working with the German development agency, GIZ, on developing entrepreneurship courses and drawing on German experience. The State Employment Service has integrated and adapted the internationally tried and tested ILO modules Start Your Own Business and Know about Business[6] and is exchanging information and experience on self-employment programmes with the employment service of Ukraine.

The participation of women in entrepreneurship in Azerbaijan is still below the level of some of the other countries, but Azerbaijan is catching up through a series of measures to promote women's entrepreneurship. The state systemically supports gender equity in Azerbaijan by implementation of state programmes, establishment of the State Committee on the Issues of Family, Women and Children, "engendering" various parts of national legislation, *e.g.* employment and education, and active co-operation with international organisations and networks to support gender equity programmes and policies. Government support measures in particular cover increasing women's self-employment and engagement of women in business activity. These measures are also co-ordinated by the State Committee on the Issues of Family, Women and Children. There are a number of successful examples of holding public events, training programmes jointly organised by civic interest groups and the government in Azerbaijan, both in the capital and in the regions. A recent development at the national level is the establishment of the Union of Women Entrepreneurs which contributes to policy partnership for enhancing women's opportunities as contributors to national growth and competitiveness. It is important to continue these efforts to establish a structured social dialogue and national partnership, adoption of targeted national policies and dedicated programmes to support the entrepreneurial activities of women and raise society's awareness of women's entrepreneurship as an important economic and growth objective.

The area of non-formal learning is also developing. The Adult Education Association, already mentioned, brings together private and public actors. The Baku Business Training Centre provides different types of training courses in different parts of the country, based on a regular local Training Needs Analysis. The State Employment Service provides support

through open youth clubs to activate young jobseekers to work towards employment. This includes self-employment. Twice a year the employment initiative, First step in career, is announced on TV. Internet TV YURD (*www.yurd.tv*) regularly reports on entrepreneurship initiatives. The state employment service is running a programme with the support of the World Bank Social Protection Development, for people who want to start their own business. NGOs are also active in providing entrepreneurship courses throughout the country, particularly for specific target groups such as displaced persons. There are TV programmes covering the good practices of small businesses: for example, "Quality Sign", "Village Hour" (on farmers' experiences) and entrepreneurship courses are advertised.

The Ministry of Education oversees the quality of education and training, and has started an ambitious programme for the accreditation of public and private providers. On the practical level, preparations for a national system for the quality assurance of training programmes are still at an early stage, although the Baku Business Training Centre has established clear principles for quality assurance of the courses it is delivering by insisting on trainers with international certification and the systematic evaluation of courses. Various international programmes have their own built-in quality assurance instruments. ILO's courses, Start your business, Improve your business, etc., are adapted to international standards although their coverage is limited. Training of trainers (ToT) has been implemented to ensure the quality of courses organised in co-operation with international partners: some examples are a ToT programme with GIZ (2010-11); ToT within the framework of co-operation with ILO (three courses on starting, organising and developing a business) and a number of short-term courses.

No data are available for training on start-ups. State support for training, infrastructure development and information and business-consultation services for growth enterprises is carried out within the general framework of SME development. There are no special policies dedicated to the support of growth enterprises, but specific evidence must be collected on the provision of training and business advisory services to growing enterprises so that financial and training support can be further tuned to the specific needs of enterprise growth in the country. A significant step in improving access to training opportunities was made in 2012 with the introduction by the Baku Business Training Centre (BBTC) of online training for SMEs. Two distance learning courses on Potential Exports Markets and Production of Organic Agriculture Products have been offered through BBTC, which has benefited more than 80 entrepreneurs from four regions of Azerbaijan.

Enhancing SME competitiveness

Business information and services

In Azerbaijan, business services are provided by both government agencies and through donor-funded programmes. The BBTC, established in 2007, operates under the Ministry of Economic Development and provides basic business information, consultancy services and training to businesses. It has six regional offices throughout the country. The BBTC also co-operates with the German International Cooperation Agency (GIZ) in the area of management training and provision of courses. The National Fund for Entrepreneurship Support complements its microfinancing with business services and support in the preparation of business plans. The Azerbaijan Export and Investment Promotion Fund provides support to firms in finding partners, and conducting analysis of potential export markets. Unfortunately, there is no information on the effectiveness of these activities and it is not clear to what extent small business benefits from these services.

Public support is complemented by donor-funded programmes such as Turn Around Management (TAM) and Business Advisory Services (BAS), an initiative of the EBRD that provides easier access for SMEs to consultancy services and international expertise. The World Bank, within the framework of the Second Agricultural Development and Credit Project, has supported, among other components, the establishment of regional advisory services for farmers. These services give farmers easier access to rural business and agricultural support such as information and advisory services.

Small businesses or entrepreneurs can obtain access to business information at the regional offices of BBTC as well as at business information centres within the framework of donor-funded programmes. A specialised website for businesses (*www.biznesinfo.az*) offers business-related information, including how to do business, current legislation and a list of businesses registered on the website, sorted by the types of services they provide. The website focuses on news, rather than on legislative developments or practical information on how to conduct a business, but it does have a question and answer communication tool. The web portal of the Ministry of Economic Development (*www.economy.gov.az*) also provides useful information to small businesses and entrepreneurs.

In Azerbaijan, there are no special initiatives that provide business support to start-ups, but they have access to the same services as other firms. According to government sources, in 2011 the BBTC provided 1 237 consulting services for start-ups and businesses across the country. Business incubators are only now being considered.[7]

Public procurement

Public procurement in Azerbaijan is regulated by the Law on Public Procurement which was adopted in 2001. Even though there is no special mandatory rule regarding the cutting of tenders into lots, the latter is reported as widely used. The legislation facilitates joint tenders and evidence of implementation is reported by the State Public Procurement Agency.

There is no separate legislative framework for combating late payment. The law does not discriminate against foreign economic operators. Buyers are required to set a proportionate qualification level and financial requirements, but there is no information as to the level of implementation of this rule.

Information on public procurement opportunities is centralised at national level and is free of charge on the website: *www.tender.gov.az*. The e-procurement system is not yet fully operational; only basic information on tenders is provided in an electronic format, but progress is ongoing to introduce e-procurement.

Innovation policy

Innovation policy in Azerbaijan is developed and implemented by the Ministry of Communications and Information Technologies, Ministry of Economic Development and the Azerbaijan National Academy of Sciences. However, innovation does not feature as a central focus of the policies and programmes developed by these institutions. The development of a comprehensive innovation strategy, with clear information on implementation plans, budgetary allocations and timelines for completion, is a necessary first step to enhance innovation and technology transfer in Azerbaijan. Greater collaboration and co-ordination across public institutions are also needed to develop an efficient and coherent approach to innovation policy and to avoid any overlap of policy actions. Currently, a law on innovation activities is being prepared by the Ministry of Economic Development.

A number of pilot projects and schemes to provide support for innovative enterprises are currently in place in Azerbaijan. For instance, the Ministry of Communications and Information Technologies is in the process of establishing Regional Innovation Zones, which will provide SMEs with access to technology parks and innovation centres focused on the ICT sector. The National Academy of Sciences has also established a Science Innovation Center in Baku to support the innovation process and technology transfer from abroad. However, participation in collaborative research projects by the private sector remains limited. Strengthening links between publicly funded R&D institutions and the private sector would lead to greater knowledge sharing and partnerships between research centres, SMEs, and other key stakeholders.

In recent years, the government of Azerbaijan has established a number of funds to support the development of scientific and entrepreneurial ventures. Financial support for innovative entrepreneurs and SMEs is available through the Science Development Fund and the National Fund for Entrepreneurship Support. However, such financial support schemes are limited in scope, and SMEs would benefit considerably from a broader range of funding schemes. Active policy measures may also be used to introduce a wider range of innovation support services, including business planning, consultancy services and technical assistance.

Green economy

The national programme on Environmentally Sustainable Socio-economic Development (2003-10) approved by the order of the President of the country dated 2003 identifies environmental measures taking into account also the interests of SMEs.

The Ministry of Ecology and Natural Resources (MENR) provides methodological support with the objective of greening of the SME activities. Furthermore the "Centre for a cleaner production and energy efficiency" is operating, which aims to create conditions to increase the energy efficiency and introduction of "Cleaner Production" concept in production, agriculture and households.

Information on environmental problems as well as the results of environmental monitoring are provided by the mass media and the continually updated web page of the MENR. MENR promptly responds to requests of SMEs on these issues. During visits to SMEs, representatives of the MENR regularly provide information about available environmental management systems (EMS). The government provides information on the EMSs to SMEs, but no support measures are in place for SMEs to apply for certification. Currently, approximately 100 SMEs have an ISO 14001 certificate.

Export promotion

Export promotion activities in Azerbaijan fall under the responsibility of the Azerbaijan Export and Investment Promotion Agency (AZPROMO), which was established by the Ministry of Economic Development in 2003. The agency's primary role is to increase non-oil foreign direct investment and to expand the non-oil export capacity of the country. Close co-operation with the private sector allows the organisation to act both as an advisor and as a government agent in implementing new business initiatives. The agency provides support to firms in finding partners and conducting analysis of potential export markets. The agency provides the following services: trade information, marketing support, information supply, consultancy and legal advice, facilitation and logistics support, as well as training. The website *b2b.az*, established with the support of GIZ, allows the firms, specifically small ones

that do not have access to information and business networks, to find business partners. In 2011 the agency also covered costs for the participation of firms in various exhibitions in Germany, USA, France and the Russian Federation.

The target group of the agency is both the existing and new exporters, and is selected based on the specific characteristics of the business and its potential for attracting investment or exporting, independent of the firm's size. No information is available on the number of small businesses supported.

An Export Promotion Programme (2011-13) was adopted by the Cabinet of Ministers in 2011. The action plan envisages the improvement of the legislative framework related to exports, strengthening the co-ordination of export policy by AZPROMO, encouraging production of quality goods for export, improving the export infrastructure and the system of quality control, and finally, export promotion and increasing awareness of entrepreneurs about export opportunities. The implementation of the action plan is co-ordinated by the Ministry of Economic Development.

Single Market opportunities

Azerbaijan has taken very limited steps towards accession to the World Trade Organization (WTO). This is a prerequisite for the EU to consider starting negotiations on a free trade agreement.

The national system of technical regulations, accreditation and standardisation represents a serious constraint for SMEs, as Azerbaijani national standards do not comply with international or EU standards. A new law on standardisation has been drafted on WTO principles, but is yet to be adopted.

The way forward

Based on the SBA assessment, Azerbaijan could consider the following steps to ensure continuing progress in the area of SME development:

- **Improving the institutional framework and intragovernmental policy co-ordination** is crucial for a more effective policy for the development of entrepreneurship. A strategic approach towards SME policy development, covering a larger number of issues, including both horizontal and targeted support, could further optimise the work of public institutions in the area of entrepreneurship support. They could then co-ordinate their various efforts in order to avoid overlap and to ensure that all crucial areas affecting SMEs are addressed.
- In order to improve the overall institutional framework and to ensure the enforcement and effectiveness of the policies promoted by the government, emphasis should be placed on **horizontal co-ordination between the ministries and agencies** involved in SME-related issues. In this way, links could be made between initiatives and projects and overlaps could be avoided.
- Azerbaijan could benefit from directing **public business support** (business services, export promotion activities, trainings, etc.) **towards entrepreneurs and small business**, as a source of new business ideas and opportunities for diversification of the economy. In particular, the definition of entrepreneurship could be broken down into smaller categories, so that various sizes of SMEs are targeted based on their specific characteristics, needs and challenges.

- **Improvement in the capacity, coverage and effectiveness of credit information system** would help to overcome information asymmetries, and establishing a central collateral registry would improve sources of collateral. This would significantly improve the ability of SMEs to access bank lending. Further improvements in the legal framework that ensure creditors' rights (to allow secured creditors to ask for creditor consents when a borrower files for re-organisation) and effective enforcement of collateral in case of borrower default are important for encouraging bank finance to SMEs.

Notes

1. *http://cpi.transparency.org/cpi2011/results/#CountryResults*.
2. For new start-ups, the criteria for classification during the first year of operation are based on the number of employees only, while for individual entrepreneurs (individuals involved in business operations without establishing a legal entity) it is based on the annual turnover.
3. Including car and motorcycle repair.
4. The Entrepreneurship Council under the President of the Republic of Azerbaijan was created based on the Decree of the President of the Republic of Azerbaijan, No. 475, dated 27 August 2002. The regulation of the Entrepreneurship Council was adopted based on the Decree of the President of the Republic of Azerbaijan, No. 867, dated 2 May 2003 (*http://e-qanun.az/files/framework/data/1/c_f_1286.htm*).
5. *www.ebrd.com/pages/sector/legal/insolvency/insolvency_sector.shtml*.
6. *www.ilo.org/empent/Projects/WCMS_143382/lang—en/index.htm*.
7. *http://pda.trend.az/en/1968428.html*.

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PART III

Chapter 15

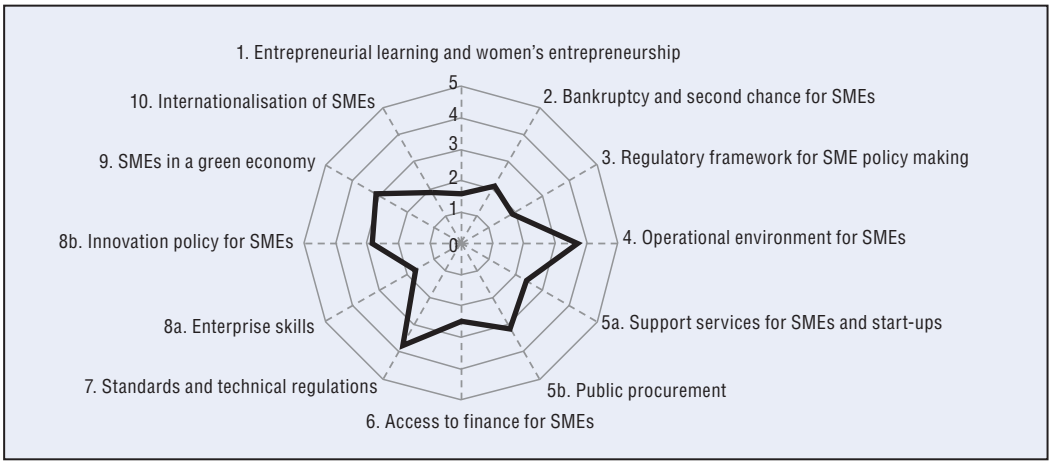
SBA country profile: Belarus*

Belarus has recently taken a more pro-active approach to supporting private entrepreneurship by promoting its small and medium-sized businesses (SMEs). The value of private sector participation in the economy is increasingly acknowledged by the government and steps are being taken to develop a comprehensive SME support policy. SME growth could be fostered through further liberalisation of economic activities which is only progressing at a slow pace.

Creating supportive policies for SMEs will only yield tangible results if progress in privatisation leads to the opening up of new business opportunities for private entrepreneurs in Belarus. Alternatively, privatisation is more likely to succeed in creating a vibrant SME sector if an enabling policy framework is in place that allows entrepreneurship to thrive.

* This chapter was prepared with the support of UNITER and Aleg Sivagrakau.

Figure 15.1. **SBA scores for Belarus**



Note: The scores for each dimension are calculated based on assigned weights for each indicator (see Annex A for further information).

Overview

This section provides a brief economic snapshot and highlights some recent trends in the business environment. This is followed by a detailed overview of the current situation of the SME sector in Belarus.

Economic snapshot

Belarus is the second largest economy in the Eastern Partner (EaP) region. It is landlocked, with a geographic area of 207.6 square kilometres and a population of 9.5 million people.

The economy is made up primarily of large industrial enterprises inherited by the state from the Soviet Union; large-scale privatisation has not yet started. State-owned enterprises generate about 70% of GDP and 50% of employment (Belstat). Key economic sectors are machine building, food and beverages and energy, followed by transport and communication as well as agriculture.

The main trading partners are the Russian Federation and the EU. In 2011, Belarus joined the Eurasian Customs Union with the Russian Federation and Kazakhstan, which is expected to increase trade between its members. The main exports of Belarus are mineral and chemical products, machinery and vehicles. Most imports to Belarus come from the Russian Federation, including cheap oil and gas which is an important growth factor supporting the Belarusian economy. The customs union agreement will guarantee a favourable price level for imported Russian gas for the time being.

In 2011, the country was severely hit by a currency crisis. Lifting currency exchange restrictions had become unavoidable but led to a dramatic depreciation of the national currency putting importers and import-dependent enterprises on the edge of survival. As the Belarusian economy is strongly dependent on imports of intermediate goods and energy resources, domestic prices also rose significantly. For 2011, the consumer price index is estimated to reach 52.9% (EBRD, 2011). The crisis had a particularly strong impact

on small businesses that were relying on the import of goods. Moreover, unstable access to foreign currency, high interest rates and a sharp depreciation of the ruble substantially hampered access to external financing by enterprises. Large state-owned enterprises could count on state support in the form of the informal system of currency distribution within state holdings or subsidised interest rates.

Table 15.1. **Belarus: Main macroeconomic indicators, 2008-12**

Indicator	Unit of measurement	2008	2009	2010	2011	2012 (proj.)
GDP growth	Per cent, y-o-y	10.2	0.2	7.7	5.3	2.5
CPI inflation	Per cent, average	14.9	12.8	7.8	52.9	56.3
Government balance	Per cent of GDP	3.4	–0.4	–1.8	3.3	0.1
Current account balance	Per cent of GDP	–8.2	–12.6	–15	–10.4	–6.2
Net FDI	USD million	2 150	1 782	1 352	3 928	2 000
External debt	Per cent of GDP	25	45.6	51.1	61.1	60
Gross reserves	Per cent of GDP	5	11.5	9.2	12.4	8
Nominal GDP	USD billion	60.8	49.2	55.2	55.5	58

Source: EBRD (2011), data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks.

Business environment trends

In recent years, Belarus has taken a more liberal approach towards the development of the private sector. The value of private sector participation in the economy is increasingly acknowledged and a number of legislative acts including the Directive of the President of the Republic of Belarus No. 4 On Developing Entrepreneurial Initiative and Encouraging Business Activity in the Republic of Belarus were adopted, setting the basis for SME policy reforms and for dialogue between state and business. Significant progress has been achieved in eliminating administrative burdens for businesses, streamlining procedures for opening a new business, and introducing electronic interaction with government bodies.

Nevertheless, liberalisation of economic activities is progressing at a slow pace, and more far-reaching reforms are required to support SME growth. The government continues to rely heavily on large state-owned enterprises rather than creating a truly level playing field for both public and private firms. In 2010, the private sector contributed to only 30% of GDP which is by far the lowest figure across the EaP countries (figures vary between 60% and 75% in the other five countries) (EBRD, 2011). Dealing with public authorities and ministries is still burdensome for businesses and many unpopular legal acts are still adopted without any prior consultation with the business community. Small businesses in particular are in a disadvantaged position compared to larger firms due to unfair competition from state-owned enterprises and a high dependence on the goodwill of public bodies.

To create more opportunities for private sector participation in the privatisation process, the government must take decisive measures to establish level playing field conditions regardless of company size and ownership status (see also Capobianco and

Christiansen, 2011, for challenges and policy options on competitive neutrality and state-owned enterprises) and create favourable framework conditions to enable private entrepreneurs to identify and realise viable business opportunities in the market.

SMEs in Belarus

The SME sector in Belarus is defined according to the definition adopted in 2009, when a new category for microenterprises was defined, in line with the EU SME definition (see Table 15.2).

Table 15.2. **Definition of micro, small and medium enterprises in Belarus**

	Micro	Small	Medium	Large
Average number of employees	Up to 15 employees	16-100 employees	101-250 employees	Firms that are not included in the definition of micro, small or medium firms

Source: Law of the Republic of Belarus of 1 July 2010, No. 148-3I, On State Support for Small and Medium Entrepreneurship.

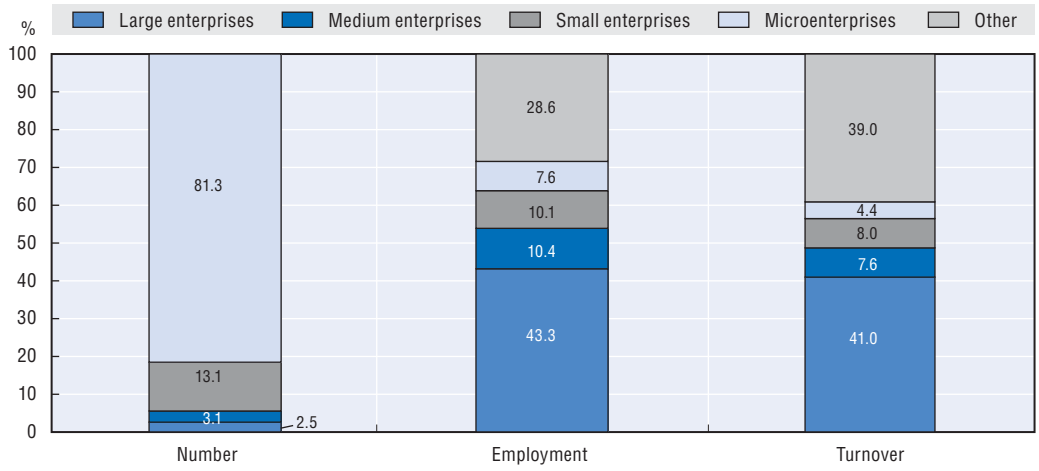
Statistics on the SME sector in Belarus confirm that the sector is highly underdeveloped. Even though 97% of companies are of micro, small and medium-size (up to 250 employees, without individual entrepreneurs) the sector only contributes to 20% of GDP and 28% of employment. This is low in comparison to other EaP countries in which SMEs, on average, contribute to about one third of GDP and about one half of employment. The data does not take into account the informal sector.

In 2010, the number of active small and medium-sized enterprises fell as a result of the crisis and unfavourable conditions for businesses operating in higher value-added sectors such as industry and production. The number of active microenterprises rose by 25% from 2008 to 2010 mainly as a coping mechanism for self-employment.

Indeed, data on the distribution of enterprises by economic sector show that the majority of microenterprises operate in lower value-added sectors such as trade (46.3%) and services (transport, storage and communication, real estate). The sectoral distribution of medium-sized enterprises is quite similar to the distribution of large companies which are more active in agriculture (28.7% and 25.1% correspondingly) and manufacturing (22.5% and 29.6% correspondingly).

Being more flexible and able to adapt to the changing situation on international markets, small enterprises did well in international trade. During the global economic crisis in 2009, Belarusian SMEs generated 37.9% of the country's exports, a share which grew to 42.9% in 2010. Such a large export share of SMEs compared to their share in contributing to the GDP is most probably explained by the fact that the main large export-oriented enterprises in oil-refining, potash and heavy machine-building industries have affiliate trading companies that correspond to the SME criterion. Therefore, the export goods produced by large enterprises are reflected in statistics as being exported by SMEs. It is also worth mentioning that enterprises with less than 100 employees generate more than one third of Belarusian exports.

Figure 15.2. **SME sector in Belarus, 2010**



Note: "Other" includes not-for-profit organisations, public bodies, banks, insurance companies.
Source: Belstat.

SBA assessment results

This section outlines the main results for Belarus from the 2012 SBA policy assessment of EaP countries. The assessed policy dimensions were reassembled and grouped under five wider SME policy areas.

Strengthening institutions and mechanisms for SME policy making

Belarus adopted a number of laws addressing SME issues, including the Directive of the President of the Republic of Belarus No. 4 On Developing Entrepreneurial Initiative and Encouraging Business Activity in the Republic of Belarus, which promotes measures of economic liberalisation and improvement of the business environment for small and medium-sized enterprises. The directive is yet to be enforced. With regard to legislative simplification, there is scope to conduct a regulatory review and guillotine of the primary and secondary legislation, and to develop a legal framework for RIA and the SME test.

Institutional framework

The institutional framework for SME policy in Belarus is in the process of formation. SME sector development has been declared a priority since 2010 with the adoption of the Law of the Republic of Belarus On State Support of Small and Medium Entrepreneurship and the Edict of the President of the Republic of Belarus On Specific Measures of State Support to Small Entrepreneurship, that set the basis for the development and implementation of an SME policy. Moreover, in 2009, the definition of an SME was changed to include a separate category for microenterprises, thereby aligning more closely with the EU definition.[1] Finally, 2011 was announced as The Year of Entrepreneurship in Belarus, underscoring once again the importance given to SMEs.

SME policy is reflected in the State Support Program for Small and Medium Entrepreneurship (2010-12) developed and implemented by the Department of Entrepreneurship of the Ministry of Economy. The intergovernmental co-ordination in SME policy elaboration is formalised through a consultation process between the ministries as part of the approval process by the Council of Ministers. The Department of Entrepreneurship itself however lacks authority in dealing with other state bodies and

ministries, and measures of the State Program for Small and Medium Entrepreneurship are often not supported by the state authorities concerned and have a nominal character.

The amount allocated for the implementation of the programme has decreased in 2011 compared to 2010, when approximately EUR 6.2 million were allocated. Nevertheless, in both years the amount has increased significantly overall, compared to 2007-09, demonstrating the high priority the government gives to the development of SMEs.

Another initiative aiming to improve the business environment for entrepreneurs is the Directive of the President of the Republic of Belarus No. 4 On Developing Entrepreneurial Initiative and Encouraging Business Activity in the Republic of Belarus. This directive addresses issues of economic liberalisation, such as private property protection and ensuring fair competition in the market between state-owned and private companies. However, the directive lacks legal power and a number of legal acts have yet to be adopted and amended to enforce the document. To reaffirm the commitment of economic liberalisation and to encourage entrepreneurial initiative the government should ensure that Directive No. 4 is enforced, by adopting relevant laws and other legal acts and revising the corresponding business legislation.

Belarus could benefit from clearer and more transparent institutional framework mechanisms for co-ordination in the area of SME policy. Currently the concentration of development and implementation of tasks in one department undermines the principle of accountability in policy delivery as there is no functioning control mechanism for transparent and objective monitoring of policy implementation. In addition, the effectiveness of state policy for SME support is undermined by the dominance of informal levers of pressure on business from the state authorities, such as rental of premises, state licensing, sanitary and fire safety norms, dependence on state-owned enterprises for supplies, etc.

Legislative simplification and regulatory impact analysis (RIA)

The provision of a clear and unambiguous legal environment represents a key priority for the government of Belarus. Directive No. 4 On Development of Entrepreneurial Initiative and Stimulation of Business Activity in the Republic of Belarus includes a number of measures to simplify and eliminate complex laws and regulations. The Ministry of Economy of Belarus has also established a working group responsible for the simplification of administrative procedures for entrepreneurs. In co-ordination with government bodies and regional executive committees, the working group has reviewed and made changes to legislation and regulations in a number of strategic areas. However, changes to laws and regulations still occur on an *ad hoc* basis, and the government has not developed any comprehensive plans to simplify current business-related legislation and to reduce legislation related to SMEs.

In addition, Directive No. 4 calls for "mandatory public discussion of draft legislative acts". However, the directive lacks legal power and the government of Belarus has not undertaken steps to include RIA in the current legislative framework. In addition, there is no formal requirement to conduct the SME test and to consider the impact of draft laws and regulations on SMEs.

Public-private consultations (PPC)

Public-private consultations in the Republic of Belarus are set up within the framework of two advisory councils, a Commission on Support to Entrepreneurship and as sections on official web pages of state authorities with the drafts of legal acts proposed for discussion and comments.

The two advisory councils concerning SMEs, the Advisory Council on Entrepreneurship Development within the Council of Ministers and the Advisory Council on Entrepreneurship, Investments and Innovation within the Ministry of Economy, are represented mainly by governmental officials and large businesses, but also other key stakeholders such as venture capitalists, marketing experts and inventors. Despite internal regulations stipulating the frequency of sessions, meetings are held on *ad hoc* basis and there is no public information about upcoming meetings. The meetings of the advisory councils are open to any interested participants. However, in practice representatives of the business community are not motivated to participate as they do not believe that their concerns will be taken into account. In addition, the decisions of the council are advisory in nature and formal.

On the other hand, there has been some progress in the sphere of PPCs. For example, many of the points of the strategic document of the Belarusian business community, National Business Platform of Belarus, were reflected in Directive No 4. In March 2012, the government adopted a legal act that regulates the activities of the advisory councils. The business community was also asked to submit the entire alternative draft law on self-regulating organisations to the Ministry of Justice. The Commission on Support to Entrepreneurship within the Ministry of Economy, which is governmental in nature, was recently expanded with the inclusion of representatives of the business community. The commission is also quite effective, given that its activities are based on a special governmental regulation and its meetings are held once every one to two months. Other ministries and local authorities have also established advisory councils to consider different business-related issues.

Establishing a conducive operational environment

Significant progress has been achieved in promoting fast and efficient registration procedures for entrepreneurs in Belarus, and developing functional e-government services that allow for online submission of tax returns, VAT and social security returns.

Company registration

The government of Belarus has also introduced substantial reforms to the company registration process. Specifically, Presidential Decree No. 1 On State Registration and Liquidation (Termination of Activities) of Economic Entities requires just one working day to issue the company registration certificate. Together with the time needed to obtain approval of the company name by the Registry Office and open a temporary bank account, a total of three days and three administrative procedures are required to obtain a company registration certificate.

One-stop-shops for company registration are also established under Decree No. 1. According to the legislation, registration with the Unified State Register of Legal Entities and Individual Entrepreneurs must be completed within one working day of submission of all required documents to the State Registry. An additional four days are required for the State Registry to notify the tax authorities, state statistical authorities, the Social Security Fund and the Belarusian Republican Unitary Insurance Enterprise of the newly registered enterprise.

The provisions for a new online registration system have been established under Decree No. 5 On the Introduction of Amendments and Additions to Decree No. 1 of 16 January 2009, dated 27 June 2011. The website for online registration was expected to be operational for the registration of entrepreneurs on 1 September 2011; however its implementation has been delayed.

In Belarus there is no separate law on the silence-is-consent principle, and it is not used as a standard administrative practice. Including the silence-is-consent principle in the law on registration would send a clear signal to companies that registration procedures will be conducted within a reasonable timeframe, leading to a reduced administrative burden for SMEs.

Interaction with government services (e-government)

Electronic filing of tax returns, VAT and social security contributions has been available in Belarus since April 2009 for all categories of taxpayers. As of January 2011, 46 833 firms were subscribed to the online tax declaration system. Online filing of pensions is also available in Belarus. However, there is a clear need to design and develop a broad and inclusive strategy for the provision of e-government services, such as online reporting of enterprise statistics, cadastre and procurement. In addition, the government would benefit from increasing the sophistication of current e-government systems to allow for credit and debit compensation.

In December 2009 the government of Belarus approved the Law on Electronic Document and Electronic Digital Signature, which includes formal measures to allow for the establishment of e-signature accreditation bodies. At present e-signature is available for use in a limited number of areas, for instance with the tax authorities, social insurance funds and customs authorities.

The government has also established a Unified State Register of Legal Persons and Individual Entrepreneurs. An automated system of data exchange enables communication between the state registry and various public authorities. This has led to substantial improvements in public service delivery, and simplifies administrative procedures for entrepreneurs involved in the company registration process.

Bankruptcy procedures and second chance

The legal framework for dealing with distressed companies, receivership and bankruptcy in Belarus is represented by the Law on Economic Insolvency (Bankruptcy) of 18 July 2000 and a number of Presidential Edicts. The Belarusian approach to bankruptcy procedures has certain peculiarities. For example, not getting paid is not sufficient reason for a creditor to initiate a court bankruptcy procedure. A creditor must first prove through court examination that the company is insolvent according to certain criteria and a court-established plan for settling relations between the economic entities must have failed before formal bankruptcy proceedings may start. Moreover, strategic state companies (such as city-forming enterprises or enterprises processing state or international orders) cannot be subject to liquidation procedures and can only be financially rehabilitated. Only 3.6% of total bankruptcy cases as of the beginning of 2012 concerned state-owned companies. This confirms that bankruptcy procedures are not systematically applied regardless of ownership status or importance to the national economy.

Belarus has no special policy measures regarding second chance for failed enterprises such as information campaigns, round tables, etc. On the other hand, there is currently no official register or database which lists companies that have undergone bankruptcy procedures (the state programme E-Belarus provides for the creation of such a register in the future). Thus, there is no indication of companies that have undergone a financial rehabilitation process in any official information resource and discharge from bankruptcy can be considered automatic. The legislation helps distressed companies to settle debts

more quickly to the extent that tax debts take 3rd priority and fines for delayed taxes take lowest priority in the order of debt settlement. However, creditors take a lower priority than tax debts, even if obligations are secured through pledge. The state support and public procurement regulations do not contain discriminatory provisions regarding re-starters. Moreover, companies that are in the process of financial rehabilitation within the framework of the bankruptcy procedure are not excluded from participation in public procurement.

Facilitating SME access to finance and developing the legal and business environment

Banks and one microfinance institution are the main sources of external financing for SMEs. Bank lending has been affected by the recent currency crisis. Although an SME support programme has been adopted, government financial support of SMEs remains very limited. Equity finance remains weak but awareness of it has increased as a way of raising capital. The legal framework has improved in recent years, particularly as regards property registration. A cadastre system is in place but the process of registration of movable assets is not fully developed. Public credit information services, though accessible, remain costly for the public and the rights of secured creditors should be strengthened.

Sources of external finance for SMEs

SME finance in Belarus is principally provided by commercial banks but on a relatively limited scale. Banks are usually more reluctant to lend to SMEs than to large businesses and this is especially evident in rural areas. Credit to the private sector accounted for around 42% of GDP as of December 2011. The banking industry lacks competition and is dominated by Belarusian and Russian state-owned banks. Priorbank is the only privately-owned bank amongst the top five players. Bank lending was particularly affected by the deep (policy-induced) balance-of-payments crisis in 2011. Credit growth decelerated and non-performing loans increased, disproportionally affecting SMEs' access to finance. Now that the central bank has tightened monetary policy, curbed directed lending and unified exchange rates in October 2011, the economy is stabilising. The 2012 medium-term strategy for attracting foreign investments envisages privatisation in the banking sector.

Access to finance through leasing has been growing actively in recent years and in 2010 the leasing portfolio of Belarus was estimated at around 3% of GDP. Following regulatory amendments adopted in July 2010, leasing activities are currently regulated by the Civil Code except in cases provided by a decision of the president or applicable law. To date, no particular leasing supervisory body has been created in Belarus.

Microfinance in Belarus is provided mainly by banks and one microfinance institution which has recently been created for this purpose. EBRD and other international organisations have helped develop bank lending to SMEs. The programme on Microfinance Development 2010-15 supported by the United Nations Development Programme (UNDP) that led to a draft MFIs regulation has raised awareness of entrepreneurs on the availability of funding. This in turn has led to an increased interest in SME loans. On the other hand, the macroeconomic conditions, particularly deep devaluation and hyperinflation have significantly diminished local market opportunities for SMEs thus depressing growth and hence demand for new lending in 2012.

Other sources of finance, such as private equity and capital markets, are in the early stages of development. The private equity sector is yet to develop and there is little

interest, including from regional international private equity funds. Securities market legislation is undeveloped. The government primary bond market shows a reasonable level of development but the public equity market is very small and not cash convertible.

Government financial support of SMEs remains very limited and several areas of state involvement could be improved, including the transparency of the selection process of state-supported recipients, the burdensome bureaucracy and the absence of a systematic approach to SME financing. Nevertheless, there is an increasing awareness of this issue and a government programme to assist the SME sector for 2010-12 has been developed. Start-up public funding is restricted to unemployed individuals with a particular focus on rural areas.

A business angels network is being developed in Belarus, although the government does not specifically sponsor any such initiative. The Business Angels and Venture Investors Network (BAVIN) was registered in November 2010 as a privately-funded organisation and currently comprises 11 business angels. The network has engaged in high-profile activities such as the programme Promote by teaching which provides training to managers on the operations of start-up businesses.

Legal and regulatory environment

A National Cadastral Agency is in place and now offering access to online services as a unified state register of immovable properties and a register of administrative and territorial units. The time and cost of registration has decreased significantly and, as a result, land registration has increased considerably in the past two years, by about 60% in 2011 alone. In 2008, the Law on Mortgages was adopted, which provides a systematic regulation of mortgages (especially of residential real estate) and legal basis for long-term mortgage lending. These improvements facilitate the use of the mortgage as a security for credit. With respect to movable assets, a registration system is operating for vehicles belonging to legal entities and individual entrepreneurs. However, rules on the registration of security interests over other types of assets are not fully implemented.

Public credit registry is in place and the extent and accuracy of information has improved since 2009 when the minimum threshold for loans recorded in the database was eliminated and borrowers were allowed to review the information. Credit reports are available to banks and to the public, including individuals and legal entities. Credit reports on third parties are provided subject to a fee, except in cases where they are requested by state authorities.

The collateral required for lending to SMEs is relatively high. Bank loans are generally secured by a pledge representing a value ranging from 150% to 200% of the principal loan amount. However, there are flexible requirements for loans of less than USD 30 000 and a lower collateral coverage is required for loans below a principal amount of USD 25 000.

Legislation on creditor rights requires owners of a legal entity which files for re-organisation to notify the entity's creditors in writing. Each creditor has the right to demand termination or early performance of the debtor's obligations and may claim for damages suffered as a result of such termination. However, secured creditors are not the first to be paid from the proceeds of liquidation of a bankrupt firm. They are also unable to seize collateral after re-organisation. Since 2011, the legal framework provides for out-of-court enforcement of the pledge on default.

Other factors that affect demand and supply of finance

Although some programmes such as a project by the UNDP and the National Bank of Belarus on financial education for low income families have been established, no national strategy is in place to assess financial literacy or to promote financial education programmes.

Promoting a culture of entrepreneurship and skills development

State support measures under the President's 2010 Directive No. 4 and the announcement of 2011 as the Year of Entrepreneurship in Belarus represent a significant shift in the state policy in favour of the development of a more creative, innovative and entrepreneurial society and for increased awareness of the importance of entrepreneurial culture for liberalising and boosting the national economy. While these measures stimulate the development of an entrepreneurial mindset in Belarus, they do not include actions for promotion of entrepreneurial learning in the education and training system to enable it to move from *ad hoc* public and private initiatives to a national policy framework for lifelong entrepreneurial learning (LL EL).

Entrepreneurial learning (EL) is currently being provided in Belarus in two forms. On the one hand, Belarus has made significant progress by introducing elective curricula on EL in secondary schools, from grades I to XI. On the other hand, there are school and project-based practices which often do not benefit from state support: courses and programmes at the tertiary education level, vocational education and training, publications of methodological materials on entrepreneurship, etc. Therefore, now is the time for stakeholder dialogue at the national policy level to discuss the country's needs and what support measures are required for promoting entrepreneurship as a key competence (improvement of education curricula, teacher training, introduction of active learning methods for youth and lifelong learning opportunities for other groups).

Defining roles and functions in EL policy partnership, bringing together public and private stakeholders, encouraging dialogue aimed at a structured lifelong EL policy framework – all this is needed to consolidate the individual efforts. There are examples of initiatives carried out by public and private partners (*e.g.* awards for young entrepreneurs from high-tech, venture capital and business angels' organisations), as well as consultative structures that are discussing elements of entrepreneurship promotion. While there is no dedicated partnership mechanism for monitoring EL development, advising on policy improvement measures and the exchange of good practice, existing institutional structures at the national level could consider putting EL issues on their agenda (*e.g.* the government's Advisory Council on Entrepreneurship Development or the Commission on Support to Entrepreneurship).

Public-private partnership is also needed to oversee and bring together various efforts by public and private non-formal learning providers in Belarus. These range from VET and higher education institutions, teaching *ad hoc* or demand-driven courses beyond their regular curricula, to various courses and training programmes. An open dialogue with/among non-formal learning providers would consolidate support measures, ensure effective information dissemination, contribute to the quality of training provision, and help raise awareness among the broader public of the available learning opportunities across the Republic of Belarus.

In 2009 Belarus ranked 3rd among European and Central Asian countries in women's ownership of firms (according to the WB Enterprise Survey, p. 2[2]). Gender equality, equal access to employment opportunities for women, including self-employment and entrepreneurial activities are all guaranteed by the country's legislation. Although there are no special provisions for state support of women's entrepreneurship in the Republic of Belarus, there are various *ad hoc* initiatives, *e.g.* microcredits for women entrepreneurs in Minsk City in co-operation with Belgazprombank, as well as activities within various international projects.

Women's entrepreneurship could be a much greater contributor to national economic growth, following adoption of a policy framework, approval of targeted government support measures and allocation of public funds. However, this would require the government, women's entrepreneurship organisations, business support structures and civic interest groups to engage in a policy partnership, based on experience of the national women's entrepreneurship forums over the last decade in Belarus. In this way they could reach a common understanding of the policy goals and actions for support to women entrepreneurs that would be most relevant to the country's socio-economic development. Women's entrepreneurship policies currently are not monitored by the national statistics offices- there is no data on enterprises owned by women or information on the state measures for training or financial support to women entrepreneurs. This issue requires additional discussion on what statistical evidence is needed so as to initiate implementation and monitoring of dedicated women's entrepreneurship policy measures in the future.

In recent years, support to SMEs and entrepreneurship in Belarus, including training and consulting services, has become a national priority. This is reflected in the national sustainable development strategy, the country's directions of socio-economic development, etc. The state budget is financing the development of information systems for SME access to financial support opportunities, availability of training courses, support services and databases of legislative and regulatory documents. There is a large number of training providers for small business in Belarus (54 operating business centres), and the employment centres carry out government-funded training to the unemployed, including training on how to start your own business. However, there is more evidence on provision of consultative support to entrepreneurs than on training for SMEs. A number of web resources are available for SMEs: the Ministry of Economy maintains an online register of centres for business support and incubators for small business, both in the centre and in the regions. Online courses and consulting services are available on the web. For example, the business incubator Technological Park Mogilyov provides two distance learning courses, one on innovation management and the other on foundations of energy saving.

Analysis of the training needs of enterprises is conducted on an *ad hoc* basis: *e.g.* by training providers, associations of employers, groups of stakeholders, based on the territorial principle, within projects and initiatives. Although the dialogue on various aspects of SME training provision is ongoing between the government, social partners and the business community, it has not yet addressed the issue of establishing a systematic training needs analysis (TNA) framework for the small business community. Regular and systematic data collection on training needs of the small business community is much needed.

The government of Belarus attaches great importance to its quality of education and training, but mainly within the formal system of education. According to the Code of Belarus on Education, all educational institutions including those for "additional" adult

education are subject to accreditation. Since all specialisations, educational profiles and educational fields are also subject to state accreditation, this has been mentioned by stakeholders as a restrictive factor in terms of flexibility of forms and types of training provision. Quality assurance (QA) of SME training is mostly dealt with by the business community and by private training providers, and takes place on an *ad hoc* basis, using a variety of tools (attestation of trainers, joint certificates, affiliation of schools, membership, accreditation with international organisations or networks, etc.). The SBA assessment suggests the need for dialogue among training and education providers, their clients, government, the business community and other stakeholders to discuss the objectives, principles, forms and tools of quality assurance that would be most effective in the Belarusian context and that would correspond to the country's skill development needs. There is also the need for an overall discussion on the common definition of the quality of education and training.

Since no data are available on the provision of training for start-up companies, it is hard to find evidence on the ratio of newly created enterprises that have benefited from training. Data collection mechanisms need to be put in place in order to monitor the provision of training and support to newly registered start-up companies, both for policy-making purposes and for improvement of the quality and effectiveness of service provision to SMEs.

Similarly, state support to training, infrastructure development, information and business-consultation services for growth enterprises is carried out under the general framework of SME development. Specific evidence needs to be collected on the level of provision of training and business advisory services to this group of growing enterprises. Only then can Belarus further tune financial and training support to the specific needs of enterprise growth in the country.

Enhancing SME competitiveness

In Belarus there is a limited number of policy tools directed towards improving the competitiveness of SMEs and entrepreneurs. It is important to highlight the State Program of Innovation Development for 2011-15, and a large infrastructure to support innovative SMEs. Greening the economy is also taken into account in the basic strategic documents. A more strategic approach could be taken for the provision of business services to SMEs and special support for SMEs that are exporting.

Business information and services

The Law of the Republic of Belarus of 1 July 2011 On Support of Small and Medium Entrepreneurship establishes the framework for the activities of business support organisations and business incubators. The Ministry of Economy is responsible for its implementation. However the provision of support services to SMEs does not follow a strategic approach and no analysis of market failures is conducted in advance.

The existing system of SME support services in Belarus is presented by *www.svoedelo.by* and a network of registered SME support organisations. The network includes 60 SME support centres and 14 business incubators (as of 3 November 2011). The SME support centres provide mainly consulting services on how to deal with state authorities, and conduct training and seminars. Some centres, especially in Minsk, provide their clients with more specialised services such as legal services, consultation on customs legislation, labour security, etc. These services are often provided free of charge.

Personalised services (such as development of a business plan or feasibility study) are provided on a fee basis. The private market of business services providers is not well developed, due to state licensing of such activities as printing and publishing, insurance, communication, legal and educational services, and because outsourcing of business services is not widespread.

The national portal *www.svoedelo.by* (as well as the site of the Ministry of Economy) contains extensive information on how to do business in Belarus, as well as an annotated list of SME support organisations with contact information. This information is limited to SME support organisations registered as such with the Ministry of Economy.

Belarusian SME legislation provides no definition or special approach for start-ups. Therefore, all state support for start-ups is contained within the framework of the State Program of Support to SMEs for 2010-12. Advisory services are offered to start-ups by SME support organisations and incubators. For example, in 2010, 47% of SME support organisation clients were persons who are willing to start or have just started a business.[3] There are no special financial tools for start-ups in Belarus. Small business incubators can offer lower market-rate rent on a competitive basis for innovative, energy-saving or export-oriented start-ups. In 2010, 8.5% of SMEs located in business incubators were innovative.[4]

Public procurement

The Public Procurement law envisages division of tenders into lots and enables participants to submit bids for any of them. Moreover, according to a draft law on state purchases, if a particular lot is lower than 10% of the total volume of the tender, only SMEs may participate in the bidding process.

No proportionate level of skills and financial requirements are applied. Joint bidding is not allowed.

With regard to combating late payments, it is reported that this item falls within the scope of budget legislation, but no further details are provided.

It is not clear to what extent public procurement is open to foreign operators. It seems that several restrictions are applied limiting access to public procurement by a requirement of compliance with the Regulation on the Procedure of Selection of Supplier. In certain sectors the Belorussian supplier is preferred.

Information on procurement is available online on the Internet website of the National Centre for Marketing and Price Study (*www.icetrade.by*). The system contains information about purchasing procedures in the Republic of Belarus as well as in some foreign countries (countries of the CIS, Eastern and Western Europe, the Middle East and Latin America).

A legal framework is being developed to address e-procurement solutions (electronic auctions).

Innovation policy

According to the organisational structure of the National Innovation System of the Republic of Belarus, innovation policy is regulated by the President of Belarus, the Council of Ministers, state administration authorities, the National Academy of Sciences, the State Committee on Science and Technology (SCST), and local government agencies. The SCST is responsible for the co-ordination and implementation of state policy on science, technology, innovation and intellectual property rights.

The innovation strategy for Belarus is outlined in the State Program of Innovation Development for 2011-15. The strategy outlines specific actions to support the development of innovation policy and includes information on new projects, implementation plans, funding and timelines for completion. Elements of innovation policy are also included in other strategic documents, such as the SME Support Programme for 2010-12, the National Programme for Accelerated Development of ICT Services 2011-15. Looking forward, the government should ensure that the measures outlined in the strategy are fully implemented, and that adequate monitoring and impact evaluation mechanisms are in place.

According to the register of innovation infrastructure maintained by the SCST, there are eight technology parks, four technology transfer centres with 28 regional representative offices, five innovation centres, and 46 scientific research centres available in Belarus. In addition, the State Programme of Innovative Development for 2011-15 has outlined a clear plan to promote new scientific and innovation-based infrastructure projects. The approval of a regulatory framework for public-private partnerships would encourage greater co-operation between key stakeholders and allow for the more effective use of the existing innovation infrastructure.

Innovation support services are provided by a number of innovation and technology centres. For instance, the technology parks Mogilev and BNTU Polytechnic both provide tailored business planning and advisory and consultancy services for innovative enterprises. Direct financing for scientific research and innovative projects is also provided by some technology parks, as well as through the Belarusian Innovation Fund. In addition, BAVIN provides financial support for innovative SMEs through the creation of networks between entrepreneurs and sources of financing (*e.g.* business angels, venture capital). In practice, however, state-owned enterprises are typically the primary beneficiaries of financial and technical support services, and participation from the private sector in innovative activities and collaborative research projects is extremely limited.

Green economy

Green economy concepts are taken into consideration in basic strategic documents by the government such as the State Programme of Social and Economic Development for 2011-15 and the strategy of environmental protection up to 2025. However, clear mechanisms of promoting these strategies for SMEs are yet to be defined.

Information on environmental legislation and specific programmes is mainly provided by the government, but also by a number of NGOs. Such activities are not co-ordinated at the national level and no specific funding is available.

The government of Belarus supports the certification of EMSs in accordance with ISO 14001 requirements. Information related to environmental certification is widely available and integrated in procurement rules. Furthermore, companies with a certified EMS enjoy tax incentives. However, no specific support programmes for SMEs are available. More than 280 companies have certified their EMS in accordance with ISO 14001.

Export promotion

In Belarus the National Programme for Export Development 2011-15 sets the strategic directions for the ministries to increase exports and improve the competitiveness of Belarusian products. The programme is not financed, given that it only provides directions and not specific measures. The programme does differentiate between SMEs and other economic agents.

There are several financial support tools for exporting firms. Firm participation in exhibitions abroad can be partly funded by the Ministry of External Affairs, the Ministry of Trade or the Belarusian Chamber of Commerce. Presidential Edict No. 477 allows individual entrepreneurs to export Belarusian goods by paying only a single trading charge of BYR 35 000 (EUR 3.2), which replaces all other taxes and charges. However, this scheme is not widespread among entrepreneurs, as Belarusian goods are not competitive. Further informational support and advisory services on exporting procedures and promotion of products could encourage small firms to expand their activities abroad. The export activities of SMEs should also be promoted by abolishing the administrative barriers that disproportionately affect SMEs.

There are some national promotional events dedicated to SMEs. The greatest nation-wide contest is the annual Best Entrepreneur competition, organised by the Ministry of Economy. However, the contest is not very representative of small business as only a small number of Belarusian enterprises participate and applicants complete a lot of paperwork to apply. Among other entrepreneurship promotional events the following can be mentioned: Product of the year, Brand of the year, and Best city for business.

Single Market opportunities

Co-operation between Belarus and the EU in the area of trade-related matters is hampered by the fact that Belarus is not a member of the WTO. This is preventing the government from starting negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA). At the same time, increased trade integration between the Russian Federation, Kazakhstan and Belarus has culminated in the creation of a customs union between the three countries which came into effect in July 2010. The recent WTO accession of the Russian Federation proves that the agreements on the customs union are in line with international requirements.

Belarus is an affiliated member of the European Committee for Standardisation (CEN) and the European Committee for Electrotechnical Standardization (CENELEC), an associate member of the International Laboratory Accreditation Cooperation (ILAC) and a member of the International Organisation of Legal Metrology and the International Bureau of Weights and Measures.

Belarus has signed a number of international agreements regarding technical barriers to trade, among others in the sphere of metrology – the CIPM Mutual Recognition Agreement and the international plant protection Treaty. Belarus has developed a robust institutional framework of technical regulations, standardisation, metrology and sanitary and phytosanitary control. The national legislation is in line with international requirements.

Enterprises have access to relevant information on trade related legislation of the EU on the centralised website of the government. However, there is no special export agency and the current information system needs to be further improved.

The way forward

Based on the SBA assessment, Belarus could consider the following steps to ensure continuing progress inthe area of SME development:

- Belarus would need to create **level playing-field conditions for SMEs** that would open up new business opportunities for private entrepreneurship in Belarus. Creating supportive

policies for SMEs will only yield tangible results if liberalisation of economic activities leads to an economic environment that provides equal opportunities for all companies in the marketplace regardless of size or ownership status.

- To develop an institutional framework for SME support, the government could consider setting up **an agency responsible for SME policy implementation** equipped with a clear mandate and adequate funding. Currently, the Department of Entrepreneurship in the Ministry of Economy both develops the policy and implements policy instruments. This could create difficulties regarding accountability and transparency. Ideally, the body elaborating the policy in consultation with other public authorities would also monitor and evaluate the implementation handled by a separate agency.
- Belarus would benefit from further involving the business community in the early stages of development of new policies and drafting business-related legal acts. To foster public-private consultations and make it more efficient, a **clear legal basis for public-private consultations** should be developed to differentiate between state commissions, advisory councils, expert councils, working groups and other relevant forms of PPCs. The framework should allow flexibility in the approach and design of the PPC, but it should ensure the role of the new social partners in the decision-making process. Proper mass media coverage of PPC sessions should be ensured using Internet or television.
- **Systemic state support to the support of entrepreneurship** is needed in the medium- and long-term, including specific measures for the development an entrepreneurship key competence and the introduction of entrepreneurial learning in formal and non-formal education. Special attention should be given to school curricula, teachers and the organisation of the learning process as key elements.
- A competitive and more sophisticated banking sector and macroeconomic stabilisation will facilitate sustainable access to finance for SMEs. **Reducing administrative procedures and regulations** could increase the effectiveness of state support to SMEs. Better coverage and access to information from the public credit information system, reducing costs of access to cadastre information and the introduction of a central collateral registry would significantly improve access to finance for SMEs. Improvements in creditors' rights should allow secured creditors to seize their collateral after re-organisation and to be paid out first from the proceeds of liquidation of a bankrupt firm.
- The list of SME support organisations must be supplemented by business service providers which are not registered in the Ministry of Economy. State funds designated for SME support organisations should be distributed on a more transparent and competitive basis, extensively involving mass media. A more **strategic approach to SME support**, by identifying market failures and developing corresponding support policy tools could be considered. A definition of start-up should be enshrined in the legislation to make it possible to develop **special policy tools for start-up support**.
- **Innovation policy** could be further strengthened by encouraging participation of SMEs in the innovation process (*e.g.* through tax support schemes or by involving SMEs in budget allocation decisions) and developing closer co-operation between research institutions, universities and the private sector. This would facilitate the linking of scientific research with practical applications needed by the market.

Notes

1. In early 2011 the Council of Ministers also set a maximum level of net revenues for year 2010 for small organisations to seek state support in 2011: BYR 6 billion = EUR 1.5 million for micro-organisations, BYR 20 billion = EUR 5 million for small organisations (Regulation of the Council of Ministers dated 7 March 2011, No. 276, "On setting maximum revenue requirement for small business entities for 2010").
2. *www.enterprisesurveys.org/Reports/~/media/1941B0BE773C493E88D0291FB0DADD5D.pdf*.
3. *www.economy.gov.by/ru/small_business/support-of-small-enterprise/activities-of-infrastructure-to-support-small-businesses*.
4. According to Belarusian legislation innovative activities are activities providing the creation and implementation of innovations (in its turn innovations are new or improved technologies, types of commercial products or services, as well as organisational and technical solutions of an industrial, administrative, commercial or other nature, conducive to the promotion of technology, commercial products and services to markets). As in Belarus the status of an innovative enterprise allows substantial tax exemptions, such a company is to be recorded in a state register after passing a corresponding state examination and confirming its status as an innovative enterprise.

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PART III

Chapter 16

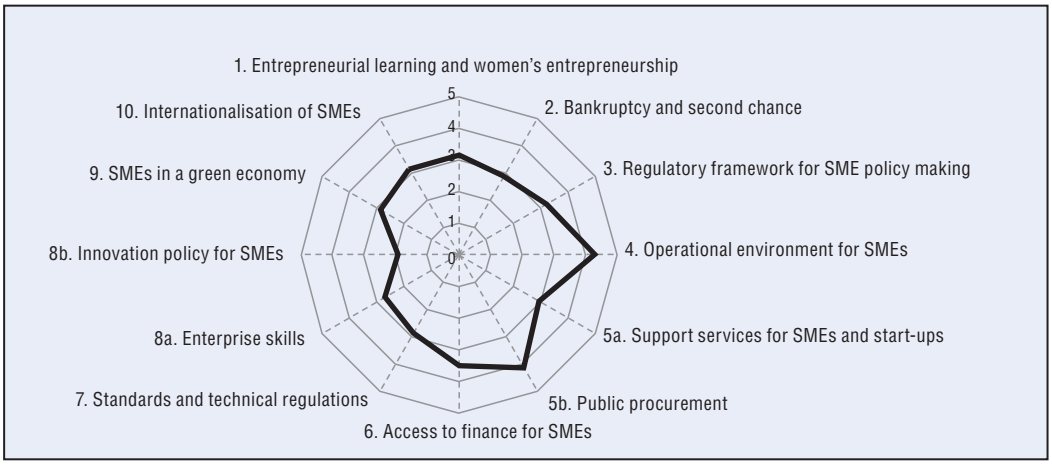
SBA country profile: Georgia*

Within its economic policy reform agenda, Georgia has improved the business environment for SMEs by simplifying administrative regulation, reducing the tax burden and fighting corruption. Liberalising conditions for doing business in Georgia include simplifying regulatory practice and facilitating free trade and privatisation campaigns. The National Anti-Corruption Strategy has been an important instrument to support businesses by introducing simple rules and overcoming administrative hurdles. The SBA assessment shows high scores for responsive administration and access to finance dimensions.

The country would benefit from a more targeted approach with a stronger focus on development of enterprise skills, innovation policy and SME support services. Currently, SMEs do not play an important role on the economic policy agenda, given their small production value and turnover, but a more pro-active approach in areas of know-how accumulation, capital investments and absorption capacities for technologies would help tap their potential. Ideally, this approach should be linked to regional development objectives and sector priorities.

* This chapter was prepared with the support of Dmitri Japaridze and Nelly Dolidze.

Figure 16.1. **SBA scores for Georgia**



Note: The scores for each dimension are calculated based on assigned weights for each indicator (see Annex A for further information).

Overview

This section provides a brief economic snapshot and highlights some recent trends in the business environment. This is followed by a detailed overview of the current situation of the SME sector in Georgia.

Economic snapshot

During the period 2004 to 2008 GDP in Georgia grew considerably, with an average growth rate exceeding 9% in 2005, and peaking at 12.3% in 2007. The August 2008 war, followed by the economic crisis, slowed down these growth trends which were later restored and led to an estimated real growth of GDP of 6.3% in 2010 and of 7% in 2011. The 2010 GDP rebound was led by manufacturing, financial intermediation and the trade sectors (GeoStat). Georgia's main economic activities include industry (manufacturing of food, alcoholic and non-alcoholic beverages, tobacco, chemical products, metals, transport equipments, machinery, etc.); trade; transport and communication; agricultural cultivation (grapes, citrus fruits and hazelnuts); mining of manganese and copper; generation of hydro-power energy; and tourism and tourism-related activities. They all play an important role in Georgia's economic growth.

Georgia has a large trade deficit due to its heavy dependence on imports, particularly oil, gas, machinery, etc. Over the past years Georgian exports have been diversified in terms of trade partners and export commodities. The largest share of exports is now processed goods instead of raw materials as in the past. Transportation and tourism are also an important part of Georgia's services exports, as the country is strategically located. It represents one of the main transit corridors for the region (three pipelines run across its territory) and is also attractive as a tourism destination. Georgia benefited from increasing inflows of foreign direct investment (FDI) in the pre-crisis period, particularly due to large pipeline projects and privatisation. FDI reached its highest level in 2007 (USD 2 billion). The main investors are EU countries. Following the crisis and the 2008 Russian-Georgian war, the levels of FDI inflows declined in 2008 and 2009, but started to recover in 2010. In 2011 FDI reached about USD 1 billion.

Table 16.1. **Georgia: Main macroeconomic indicators, 2008-12**

Indicator	Unit of measurement	2008	2009	2010	2011	2012 (proj.)
GDP growth	Per cent, y-o-y	2.3	–3.8	6.3	7	5.5
CPI inflation	Per cent, average	10	1.7	7.1	8.5	2
Government balance	Per cent of GDP	–6.3	–9.2	–6.6	–3.6	–3.5
Current account balance	Per cent of GDP	–22.6	–11.3	–11.5	–12.7	–10.3
Net FDI	USD million	1 494	659	809	921	970
External debt	Per cent of GDP	44	58	62	53.1	50
Gross reserves	Per cent of GDP	11.5	19.6	19.9	20.3	17.7
Nominal GDP	USD billion	12.9	10.8	11.6	14.3	16

Source: EBRD (2011), data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks.

Business environment trends

The reforms implemented during 2004-08 have significantly deregulated the economy, established free trade principles and created effective administration mechanisms to ensure the economic development of Georgia. Reforms, aiming at simplification of the business environment are still ongoing. The economic policy of Georgia has been focusing on opening, liberalising and fostering institutional deregulation of the economy. This has encouraged increased growth in the private sector through aggressive privatisation, reduced taxation through the introduction of a new tax code, abolishing import duties on approximately 90% of goods and a systematic reduction in the number of licences and permits necessary for doing business in Georgia. Georgia made excellent progress during 2004-10 in eliminating the inefficient legislation it had inherited, while the regulatory burden was limited to a minimum level. The World Bank's *Doing Business* analysis ranked Georgia as the number one economic reformer in the world in 2005-10 and its position improved from 112th in 2006 to 16th in 2011 in terms of ease of doing business.

SMEs in Georgia

In Georgia, the SME sector represents a large share of the business population. In 2010, 96% of 42 530 active enterprises were considered to be of small and medium size, based on the definition of SMEs set by the Law on Georgian National Investment Agency (Table 16.2). The majority are small enterprises (87.6%), enterprises registered as limited liability companies or individual enterprises. Moreover, during 2010, the increase in the total number of enterprises was mainly due to a 15% increase in the number of small firms, compared to a decreasing number of both medium and large firms. The size of the business population is based on business registry and therefore is not accurate – a large proportion of enterprises are not active.

Table 16.2. **Definitions of micro, small and medium enterprises in Georgia**

	Micro	Small	Medium
Definition 1			
Headcount		≤ 20 employees	≤ 100 employees
Annual turnover		≤ GEL 500 000 (EUR 0.23 m)	≤ GEL 1 500 000 (EUR 0.68 m)
Definition 2 (for tax purposes only)			
Annual turnover	≤ GEL 30 000 (EUR 13.5 thousand)	≤ GEL 100 000 (EUR 45 thousand)	

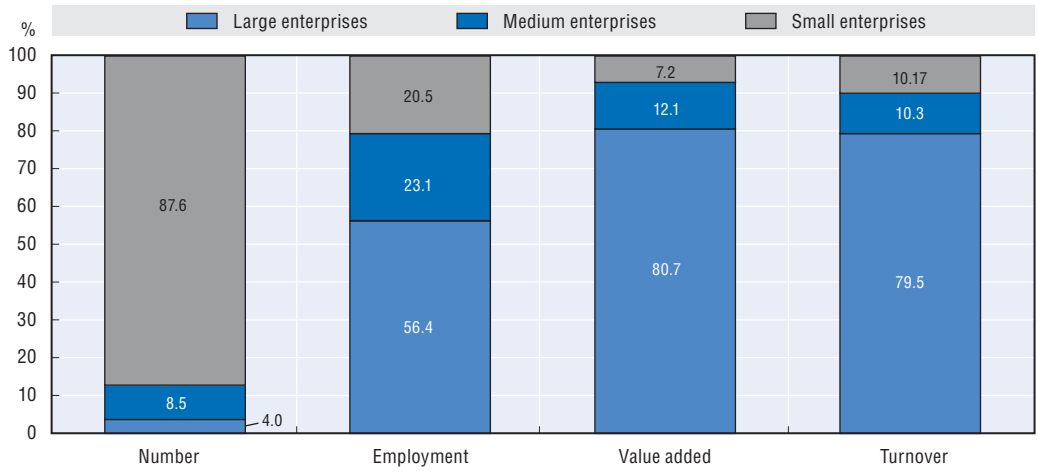
Source: Law of Georgia On Georgian National Investment Agency; Tax Code of Georgia.

Despite the growth of the Georgian economy and employment of almost half of people employed in the business sector (43.6% in 2010 and 38.3% in 2011), the SME sector still shows weak performance in terms of value added. In 2010, the SME sector in Georgia accounted for only 19.3% of value added and 16.1% of total turnover, while in 2011, the share in turnover constituted 14.4% (GeoStat). Both figures have increased since 2007, which was the result of stagnation in the large firms as a result of the crisis.

There are important disparities in the geographical concentration of enterprises across the regions of Georgia. Among the 362 683 enterprises that were registered in Georgia on 1 June 2011 (GeoStat), approximately 45% of companies were registered in Tbilisi. Tbilisi is also the undisputed leader in turnover, accounting for approximately 73% of total enterprise turnover in Georgia. The differentiation between the leaders (Tbilisi and Adjara) and the laggards is still a challenge for Georgia, but over the past years, the economic performance of several passive regions (Guria, Kakheti, Mtskheta-Mtianeti, Kvemo Kartli and Shida Kartli) has improved (Geostat).

The informal sector has been significantly reduced over the past few years as part of an extensive anti-corruption campaign by the simplification of legislative reforms. The share of the unobserved output in Georgia's total output has been reduced from approximately 32% in 2004 to 22% in 2010 (GeoStat).

Figure 16.2. **SME sector in Georgia, 2010**



Source: GeoStat.

SBA assessment results

This section outlines the main results for Georgia from the 2012 SBA policy assessment in EaP countries. The assessed policy dimensions were reassembled and grouped under five wider SME policy areas.

Strengthening institutions and mechanisms for SME policy making

In terms of an institutional framework for SME policy development, so far there have been no targeted measures. However, Georgia pursues a pro-active policy to create favourable conditions for all enterprises.

Institutional framework

The Ministries of Finance and Economy and Sustainable Development of Georgia lead and co-ordinate horizontal activities on issues related to entrepreneurship, small business and regulatory reform. At the same time, no special institutional arrangements have been created for SME policy. Line ministries communicate with each other on an *ad hoc* basis which seems to be a functioning mechanism for the co-ordination of activities within the framework of joint public projects. The Tax Ombudsman plays an important role in mediation between government and the business community and communicates with businesses on an ongoing basis.

While there is no SME strategy *per se*, the State Strategy for Regional Development of Georgia for 2010-17 states its support for the development of innovation, new technologies and entrepreneurship as one of its objectives. An action plan for the strategy has recently been adopted, and funds have been allocated, including for several measures that would target the development of entrepreneurship.

There is no single definition for SMEs which is used across all public institutions in Georgia. The main definition of SMEs, which is also used for statistical purposes, is stated in the Law on Georgian National Investment Agency. A separate definition, based on turnover only, is used for tax purposes and is in force since 1 January 2011. It is used to offer special/preferential treatment to small and microenterprises.

Anti-corruption measures are recognised as one of the most successful parts of the reform policy since 2004. The government has succeeded in reducing the shadow economy and eradicating corruption through radical law enforcement measures and tax reforms. Liberalisation of the regulatory sphere has led to a business environment free of bureaucratic pressure and administrative burden. Accordingly, Georgia has been ranked as a top reformer country by the World Bank's *Doing Business* report in recent years. Georgia has also adopted the National Anticorruption Strategy and Action Plan.

Legislative simplification and regulatory impact analysis (RIA)

Georgia has already completed an extensive review of its business-related legislation and regulations. From 2006 to 2010, approximately 21 000 legal acts were reviewed; of these over 12 000 were abolished. The legislative review and guillotine process is ongoing on a permanent basis, and is included in the Georgian National Anticorruption Strategy. The plan includes measures to streamline legislation in strategic areas such as public and administrative services, public procurement, public finance, company/entrepreneurial legislation and tax and customs systems. However, the government does not explicitly identify SMEs as a priority in the legislative review process.

The Ministry of Economy and Sustainable Development of Georgia has also established the Business Activity Regulatory Impact Assessment Division, dedicated to analysing the impact of laws and regulations on the business environment. Georgian legislation also requires that a brief assessment of the impact on key stakeholders is included with every draft law. Currently the Strategy and Action Plan of implementation of RIA in Georgia has been drafted and a pilot RIA has been carried out for several laws. A light form of RIA will be implemented based on German experience. For the purpose of RIA implementation, an intragovernmental working group will be established with the participation of different government institutions, such as the Ministry of Justice, the Ministry of Economy and Sustainable Development, the Prime Minister's Office, the Ministry of Finance and GeoStat.

Furthermore, there is no official requirement to undertake the SME test when drafting new laws and regulations, but RIA will be applied to all enterprises including SMEs, given that they constitute a significant share of the total number of enterprises.

Public-private consultations (PPC)

Despite the lack of a mechanism for regular PPCs, the business community and the public administration are maintaining frequent constructive dialogues in the areas relevant to enterprise development and growth. The consultations are held when needed (but generally not less frequently than once a month), the business community is well informed about upcoming consultations, and the outcomes of the meetings are published on the websites of their respective ministries.

Some of the main organisations representing business interests are the Georgian Chamber of Commerce and Industry, the Business Association of Georgia, the Employers' Association of Georgia, the International Chamber of Commerce, etc. Associations are organising the process of voicing business concerns in terms of legislative initiatives and other forms of policy advocacy. The recently established Tax Ombudsman's Office in particular has become the main mediator between the government and private enterprises.

Despite the active role that PPCs play in contributing to the friendly business environment in the country, small and medium-sized enterprises are not properly represented and their needs and concerns are not entirely reflected in the activities of these associations. The dialogue is mostly focused on the needs of large companies as the source of a substantial contribution to GDP. The challenges encountered by SMEs could be more actively brought to the attention of policy makers. This would facilitate participation of SME representatives in dialogue with these associations.

Establishing a conducive operational environment

The regulatory environment has undergone considerable reform and restructuring in recent years, with the result that Georgia has developed the most advanced service delivery model in the Eastern Partner (EaP) region. The integration of government services within Public Service Halls, the introduction of electronic identification cards and the development of e-government services are some of the most significant developments. Nevertheless, additional reforms are needed to introduce an online registration system, and to integrate electronic signature within the current offer of e-government services.

Company registration

Georgia has the most efficient and straightforward company registration process in the EaP region. Companies and individual entrepreneurs spend just one day to pay the registration fee, obtain a company identification number, open a corporate bank account, and obtain a registration certificate and tax registration. These procedures can all be completed at the National Agency of Public Registry (NAPR). The Ministry of Justice has also recently introduced Public Service Halls offering various services for entrepreneurs in a single location. In addition to company registration, Public Service Halls give citizens centralised access to the Civil Registry Agency, the National Archives of Georgia, the National Bureau of Enforcement, the Notary Chamber of Georgia, registration of immovable, movable and intangible assets and cadastral services.

Georgia has established a state-of-the-art company registration system, with widespread availability of one-stop-shops, and a well-functioning and efficient electronic

company register. The government issues a single identification number during the registration process, without requiring entrepreneurs to register with additional authorities. However, online registration for companies and individual entrepreneurs is currently lacking, and the government has not drawn up any plans to develop a website for online registration. The approval of a law allowing for online registration would be an important and necessary first step in this direction.

The silence-is-consent principle has been introduced in the Law on Licences and Permits, the General Administrative Code, the Civil Code, and the Law on Securities Market, which are areas where procedures take time. Silence-is-consent is not applied in case of registration, given that after the streamlining and simplification of registration procedures, companies can receive their registration immediately.

Interaction with government services (e-government)

The Revenue Service of the Ministry of Finance in Georgia has developed a sophisticated system for online filing and payment of corporate income tax, property tax and VAT. Furthermore, as part of reforms to the new Tax Code enacted in 2005, social security contributions were reduced from 31% to 20% in 2005 and were entirely abolished in January 2008. Consequently, there are no compulsory requirements for businesses to pay social security contributions from employee wages. Other e-government services are also available in Georgia, including online cadastre, procurement and customs declarations.

The development of a system allowing for online reporting of enterprise statistics is underway in Georgia, and is envisaged in the National Strategy for Statistics Development. At present, statistical surveys are available for download on the website of the National Statistics Office of Georgia (GeoStat) and can be submitted by email.

A Law on Electronic Signature and Electronic Documents was adopted in March 2008. According to the legislation, the Georgian Accreditation Center under the Ministry of Economy and Sustainable Development is responsible for the accreditation of companies and responsible for issuing certification for e-signatures. Although e-signature has not been implemented in all areas of interaction with the public administration, SMEs are able to use alternate means to validate electronic documents. For instance, the Revenue Service of the Ministry of Finance assigns a unique username and password to each taxpayer, facilitating effective online filing of tax returns. Increased implementation of the law on electronic signature would make e-government services more widespread in Georgia.

Direct connections have been established between various institutions operating under the Ministry of Justice, including the public and business registry, cadastral data, national archives and enforcement services. In addition, the database of the National Agency of Public Registry (NAPR) is fully available for use by the Ministry of Economy and Sustainable Development and the tax administration office. Electronic identification documents were also released for citizens on 1 August 2011, paving the way for further development of e-government services.

Bankruptcy procedures and second chance

Bankruptcy procedures in Georgia are established by the 2007 Law on Insolvency Proceedings. An amendment was adopted in January 2012 to further streamline procedures and speed up insolvency proceedings. The main purpose of the law is to equally protect the rights of a debtor and of a creditor, to resolve future financial problems

and, if necessary, to satisfy creditors' claims through the sale of assets (Article 1). Over the past two years, 19 companies have undergone bankruptcy procedures.

According to the EBRD Insolvency Law Assessment carried out in 2009, the law is only "low-compliant" with international standards due to a number of weaknesses, such as the lack of a "balance sheet" test for insolvency, vague pre-bankruptcy avoidance provisions and insufficient treatment of re-organisation procedures (EBRD, 2009). According to the World Bank, the 2007 law succeeded in bringing down the cost of proceedings to only 4% of the estate's value. Nevertheless, Georgia still only ranks 109th (out of 183 economies) in *Doing Business 2012* on the indicator Resolving Insolvency. This is due to the relatively long time required (3.3 years) and the low proportion of assets claimants will recover from an insolvent firm (25.5 per cent on the dollar).

In order to streamline the Law on Insolvency Proceedings (2007), the Georgian government has undertaken a follow-up reform aimed at the elimination of shortcomings that have come up in practice, as well as the streamlining of insolvency proceedings.

Public authorities in Georgia could play a more supportive role in debt settlement if tax debts were to take lowest priority in a bankruptcy. Currently this is not the case as unsecured claims and claims presented after the deadline for filing claims take lower priority over tax debts. Even secured claims take priority only if tax authorities have not registered a tax lien (Law on Insolvency Procedures, Article 40). Recent amendments to the Georgian Tax Code (Article 239) and to the Law on Enforcement Proceedings (Article 823) further weakened the position of secured creditors as tax authorities were granted the right to retroactively impose a lien based on the date a tax obligation arose and no longer based on the date a lien was actually registered against a taxpayer's property.[1]

The approach towards re-starters is non-discriminatory with regards to registration procedures. There is no bankruptcy register and companies are removed from the business registry after final court decisions. To further strengthen creditors' interests, Georgia would benefit from introducing a bankruptcy register, however, with clearly defined discharge procedures and maximum time for removal from any black list kept by public authorities.

Facilitating SME access to finance and developing the legal and business environment

Georgia has made significant progress regarding the legal and regulatory framework that supports lending to SMEs. Although public financial support for SMEs has been modest, private sources of finance such as bank lending and microfinance facilities are available. A real estate cadastre is fully operational. A central collateral register and credit information systems are in place and available to the public. The legal framework and enforcement of creditors' rights could be improved.

Sources of external finance for SMEs

Bank lending to the SME sector has increased with the rapid growth of Procredit Bank, contributing to significant competitive pressure in this segment of the market and increasing the number of banks developing SME lending. The entry of foreign banks and the listing of the largest bank, Bank of Georgia, on the London Stock Exchange in 2007 have contributed to strengthening the banking system, increasing competition and improving the range of financial services offered by banks. Nevertheless, only some financial intermediaries have developed sustainable SME lending. The banking system in Georgia is

quite concentrated. Indeed, the top five of 19 banks operating in Georgia control close to 80% of assets. Only about 21% of domestic credit to the private sector goes to SMEs as large banks that dominate the market focus on financing large enterprises. The economic slowdown and the global financial crisis have affected bank lending, particularly to small and new businesses. However, credit growth has picked up since 2010 after a contraction of 13% between 2008 and 2009. Credit to the private sector as a percentage of GDP amounted to 33% at the end of 2011.

Public credit guarantee schemes have been rather small. Some state programmes, such as Cheap Credit in 2008-09, supported the development of SMEs by providing loans to entrepreneurs on preferential terms. Credit guarantee facilities have been developed by international financial institutions. The Development Credit Authority (DCA), established by USAID, has developed different guarantee programmes in partnership with local financial institutions in order to enhance access to finance for SMEs.

Financial support for start-ups is scarce. Some public programmes are available to assist start-up enterprises but have only limited impact. Financial support to start-ups is provided by the Tbilisi City Hall under the Local Business Development Support Programme, which has made available GEL 1 million to start-ups in 2010 followed by the second largest city that also launched start-up financial support in 2012.

A business angels network is being established in Georgia. The Georgian government has also involved in a pilot project that investigated the environment in which business angels operate.

Other providers of finance, such as microfinance institutions (MFI), are important and operate throughout the country. They provide loans in both rural and urban areas across the country. Most clients are small-farmers and individuals. However, despite a well developed network and institutional structures, MFIs lack the financial capital to meet the demands of microlending. Fifty-seven microfinance organisations are currently operating in Georgia. According to the Microfinance Information Exchange (MIX) microfinance lending reached 4% of GDP at the end of 2010.

Leasing operations are gradually developing but represent only a small fraction of financing activities. The sector's penetration is 0.5% of GDP, with only three leasing companies operating in the market. On October 2011 the Parliament of Georgia adopted leasing-related amendments to the Tax and Civil Code, Law on Commercial Banks and Law on Bankruptcy, proposed by USAID experts. These amendments envisage simplifying the tax requirements in order to improve business conditions for leasing activities and to promote the acquisition of equipment and modern technologies by Georgian companies.

Private equity is in the early stages of development with very little active capital and capital available for commitments in 2010. The Georgia Regional Development Fund (GRDF), established in 2006 by Millennium Challenge Georgia, focuses on investments in small and medium-sized enterprises. The USD 30-million fund invests in businesses operating in regions outside Tbilisi and specialising in agribusiness and tourism. In March 2012, small Enterprise Assistance Funds (SEAF), within the Caucasus Growth Fund established by IFIs (EBRD, IFC, FMO, BSTDB) raised USD 42 million to boost private investment focused on Georgia and the broader Caucasus region. SEAF is the first institutional quality private equity fund dedicated to providing debt and equity capital to small and medium enterprises in the region. The aggregate capital of other private equity funds operating in Georgia is less than USD 15 million.

Although Georgia has a functioning stock exchange, the Georgian Stock Exchange (GSE) regulated by the Law on Security Markets, the level of trading activity is low even by emerging market standards. The GSE has an electronic trading infrastructure allowing for floor and remote trading by the eight registered brokers. At the end of 2011, 135 companies were listed on the GSE, with a total market capitalisation of 5.5% of GDP and a low turnover ratio.

Legal and regulatory environment

An effective National Agency of Public Registry (NAPR) is in place since 2004. There has been significant improvement in its efficiency in recent years. A computerised multifunctional countrywide cadastre and land registration system was created in 2007, which has led to rationalisation of land use and increased protection of property rights. Companies are able to obtain online information on real estate and use it in connection with bank financing.

A private credit information bureau, CreditInfo Georgia, is in place and information is accessible online. Banks, leasing companies and other organisations providing credit can access information about a potential borrower. A positive credit history is kept for seven years and a negative history is stored in the database for five years. Individuals can access their credit history and be alerted to its changes on payment of a fee.

The system for registration of movable assets is maintained by the NAPR and registrations of motor vehicles are carried out by the Service Agency of the Ministry of Internal Affairs of Georgia. The system for registration of pledges on movable property, created in 2009, enables authorised users to register such pledges online. This online registry is centralised and fully operational throughout the country. The law allows businesses to grant a non-possessory security interest in a single category of movable assets, without the requirement of a specific description of the secured assets. Any business may use movable assets as collateral while retaining possession of assets.

There are no rigid provisions applicable to collateral requirements and banks define their own requirements. These requirements are usually in the range of 50 to 100% of the loan amount, depending on the borrower's credit history and a general risk assessment.

Debtors' and creditors' rights are governed by the Law on Enforcement Issues (together with the Law on Insolvency Proceedings). The law does not allow for the suspension or cancellation of the enforcement procedures or the removal of the sequestrated property from the register list in the absence of written consent of the creditors. Secured creditors are, nevertheless, not able to seize their collateral after a filing for insolvency.

Other factors that affect demand and supply of finance

Georgia appears to be better positioned in terms of financial literacy than its regional peers. This is also evident from the individual accounts (313.2 commercial bank accounts per 1 000 adults at the end of 2010). However, this level is lower than the levels in OECD countries.

There is no national strategy on financial literacy, although certain information regarding financial products is accessible in Georgia. The Rule on Provision of Necessary Service Information to Bank Customers of the National Bank of Georgia (NBG) regulates relationships between commercial banks and their customers in relations to consumer protection.

Promoting a culture of entrepreneurship and skills development

This section considers the human capital dimensions of the SBA in Georgia: lifelong entrepreneurial learning and SMEs skills development.

Considering human resources as one of the most important pillar for a country's competitiveness, Georgia has taken steps to enhance the quality of its education and reinforce the entrepreneurial culture.

First, with the establishment in 2009 of the National Vocational Education and Training Council (NVETC) the government launched an unprecedented platform for policy dialogue and co-ordination of development of the vocational education and training (VET) sector. The participation of all relevant ministries, social partners and the non-governmental sector in the NVETC creates wide potential for structured dialogue; however the process is still in the development stage. Vocational education promotes entrepreneurial learning, teaching of a dedicated subject and support for students' entrepreneurship projects in vocational education and training colleges.

Second, a wide range of initiatives on entrepreneurial learning (EL) in non-formal learning system is provided by different national and international business development centres (IOM, UNDP, Norwegian co-operation, etc.). The Adult Education Association of Georgia gathers many national training NGOs in support of non-formal EL, social entrepreneurship (training and support to start-ups). Of importance here will be how the formal education system and the non-formal education environment could be improved and synergised. More specifically, the partnership developed in vocational education and training through the NVETC needs to be extended to other secondary levels. The non-formal initiatives would gain by becoming part of a national lifelong entrepreneurial learning (LL EL) strategy.

Thirdly, a policy framework incorporating gender-sensitive policy improvement has been approved recently, backed by an action plan (2011-13). The action plan includes specific measures supporting business education and training and proposes actions to identify and support women leaders.

Summarising, the ground is paved to build a national LL EL concept, with entrepreneurship as a key competence adequately incorporated into ongoing curriculum reforms.

The SME Skills Development dimension benefits from ongoing dialogue to establish a national training needs analysis (TNA) framework, involving the Ministry of Education and Sciences, social partners and the business sector within the NVETC thematic groups and with support of donors. These initiatives largely depend on the activities of international organisations and donors (IOM, GIZ, USAID), involving career guidance and employment centres.

In parallel, business service providers and NGOs (AYEG, USAID, IOM, UNDP, GIZ, GNIA, Georgian Rural Development Fund, etc.) cover a wide range of training for SMEs (start-up, growth, management, etc.) while the technical (trade) training for SMEs is generally provided by vocational education and training centres. The government supports online training, notably through universities. The Revenue Service (under the Ministry of Finance) conducts local seminars on taxation and micro and small business issues (according to the new Tax Code). Such seminars are planned for all regions of Georgia.

A lack of data compromises Georgia's performance, particularly on the indicators addressing start-up and SME growth training.

Georgia has a good level of quality assurance (QA) through the National Center for Educational Quality Enhancement (NCEQE), which authorises and accredits public and private training providers on a voluntary basis. Private business service providers apply their own quality assurance tools and some are certified according to international standards, such as the Georgian Federation of Professional Accountants and Auditors (GFPAA), but they can also receive accreditation through NCEQE.

The state voucher system in vocational education and training was introduced in March 2012.The vouchers can be used by beneficiaries with public and private business service providers. As it stands now the voucher system benefits learners irrespective of age or level of education, but with a preference for vulnerable groups. However, citizens may benefit from only one voucher, which limits the possibilities for continuing training.

Finally, to move forward on the SME Skills Development dimension, the wide range of training for start-ups and SMEs growth needs to be optimised through a systematic training needs analysis and a consolidated information system on training providers. This would lead to a more responsive training market and improved efficiency in the training effort to meet the evolving requirements of enterprises.

Enhancing SME competitiveness

Georgia is following a pro-active approach to enhance the competitiveness of Georgian business, but co-ordination between the various initiatives is still limited. Innovation is the focus of the current enterprise policy, and a number of initiatives such as the Technology Transfer Centre are expected to foster the development of innovative technological firms. Georgia also aims to build firm capabilities for exporting and investment.

Business information and services

The spectrum and quality of business services provided on the Georgian market have generally improved in recent years. Currently, more than 30 private business service providers are operating throughout the country. In addition, a number of programmes have been implemented by the government and donor organisations to establish SME support services. These programmes are delivered through a network of business support centres which are in most cases receiving support from donor organisations. The services provided range from informational support to the provision of equipment for rent. For example, within the framework of EBRD's BAS programmes, part of the costs for business services is covered by the programme. Other examples are Agriculture Mechanisation Centers, set up by USAID in 2010, which are equipped with various types of agricultural equipment and machinery for local farmers. Consultations for farmers were also provided under programmes implemented by CARE. As of 2012, extensive development centres have been created by the government of Georgia to provide advisory services and technical support to farmers. The various initiatives are scattered and there is no co-ordination between them to ensure efficient allocation of resources or to avoid overlap. No strategic approach has been taken to encourage the development of the private business services market, and currently the market is highly dependent on donor support.

A comprehensive guide on how to conduct business in Georgia, with detailed information about the steps required to start a business, current regulations, a list of

business services providers and other useful information, is available for download on the website of the Ministry of Economy and Sustainable Development of Georgia, as well is in paper form (brochure) at regional information centres. However, it should be noted that there is no single web portal dedicated to SMEs. Given that a website is easier to update and allows interactive activities such as forums to discuss new legislative developments or to share problems encountered in business, creating a unified portal covering all spectrums of SME-related topics could further improve access to information for SMEs. The Tax Ombudsman's Office has an online portal, which serves as a platform for businesses to send questions and to identify their problems, if any; they are responded to and addressed by the Ombudsman's Office.

There are limited support schemes for start-ups, and so far, few start-ups have been achieved. Start Business with the help of the City Hall is one of the municipal initiatives that aim to support people who want to start a business. They provide advice, information and funding. In 2011, another programme, Get employed and employ with the Mayor of Tbilisi provides financing to projects and ideas based on a competition. Kutaisi City Hall started its SME financing programme in 2012. Other organisations provide support to start-ups as well. For example the Association of Young Economists of Georgia, the chambers of commerce and industry and business associations all provide general informational support. This area needs to be strengthened in terms of expertise and better promotion among entrepreneurs.

As in the case of business services, Georgia does not have a strategy on business incubation; most business incubator projects have been initiated by international organisations. Currently, there are around 10 active business incubators in Georgia. Successful incubation projects in Georgia have been implemented by UNDP, USAID, GIZ and other donor organisations. The sustainability of business incubators is now in question because of a lack of interest on the part of those with informal venture capital which is indispensable to ensure the longevity of the project.

Public procurement

The Law of Georgia on Public Procurement allows for cutting tenders into lots which is a common practice. Furthermore, the law foresees the possibility of joint bidding. As for the setting of proportionate qualification levels and financial requirements, it is not specified whether the law provides for specific provisions related to SME, but it stipulates that the requirements for qualifications should be fair and non-discriminatory, and conducive to healthy competition. It is also specified that all documents to be obtained from public institutions shall be provided only by the winning company.

There is no specific law addressing late payment. At the same time state institutions have no problem with timely payments. However, it is not known whether this holds true in other public areas outside procurement. The e-procurement system is also linked to the e-treasury system, through which all procurement-related transactions financed through the state budget are managed.

The procurement market is fully open for foreign economic operators.

All tenders are carried out electronically, using the centralised e-procurement web portal (*www.procurement.gov.ge*). All information is freely available, including a specially dedicated helpdesk. The State Procurement Agency carries out special training for suppliers. The entire procurement system is designed to operate exclusively by electronic

means; this includes tender documentation, tender notices, annual procurement plans, bidding documents, all decision of the tender commission, all relevant correspondence and an electronic dispute resolution module for submitting complaints.

Innovation policy

The State Commission for Regional Development is responsible for the development of innovation policy and schemes to support new technologies and entrepreneurship in Georgia. The commission is chaired by the Minister for Regional Development and Infrastructure, and is supported by the Task Force for Regional Development and seven well-structured working groups. The working group on Innovation, new technologies and entrepreneurship forms recommendations for the strategic direction of innovation policy in Georgia by bringing together policymakers, experts from the task force secretariat, and representatives from Georgian universities and public institutions.

Elements of Georgia's approach to innovation policy are included in the Regional Development Strategy of Georgia for 2010-17, developed by the Governmental Commission on Regional Development. Within the Ministry of Regional Development and Infrastructure, the Department of Reforms and Innovations supports the implementation of this strategy. In addition, the National Intellectual Property Center (SAKPATENTI) implements projects in the fields of technology transfer and intellectual property rights, and the Ministry of Economy and Sustainable Development develops targeted initiatives to support innovative start-ups. However, there is currently no comprehensive innovation strategy in Georgia, and increased institutional co-ordination is needed to develop a coherent and effective strategic approach to innovation policy.

In co-operation with GIZ, SAKPATENTI opened the Georgian Technology Transfer Center (GTTC) in February 2012. Although a number of privately owned innovation and technology centres have been established in Georgia, there is limited co-operation between universities, technological centres and industry in the development and commercialisation of innovative knowledge and ideas.

There are a limited number of donor-financed initiatives in place to provide technical assistance to SMEs in Georgia. For instance, the EBRD provides advisory and consulting services to SMEs within the framework of its TAM/BAS programmes. Financial support schemes for innovative SMEs are also available through various programmes to foster R&D partnerships between scientists and industry. Examples include the Joint Business Partnership Grant Programme, supported by the Georgian National Science Foundation (GNSF) and the Science and Technology Entrepreneurship Program (STEP), financed by the Georgian Research and Development Foundation (GRDF). However, innovation support schemes are presently unable to satisfy the growing demand from the private sector for innovation support services.

Green economy

In Georgia, green growth concepts have been developed by the government and focus in particular on sustainable development and greening of the economy, eco-efficient businesses and eco-innovation.

Information on environmental legislation and specific programmes is provided by various organisations, ministries and NGOs. The government organises and supports multiple forms of co-operation such as seminars, capacity building support and various

environmental education projects. Several NGOs are providing support to farmers and entrepreneurs in bio-production.

Environmental management standards (EMS) from ISO 14000[2] are available at the Georgian National Agency for Standards, Technical Regulations and Metrology (GEOSTM). Several companies have already been certified by ISO 14000 standards and the growing focus on exports increases the popularity of this scheme.

Export promotion

Export promotion activities in Georgia have been integrated with investment promotion since 2010 and are co-ordinated by the Georgian National Investment Agency (GNIA). The GNIA was established by the government in 2002 under the Ministry of Economy and Sustainable Development of Georgia to promote investments. The export promotion activities conducted by GNIA include provision of information such as export procedures, foreign market requirements, trade regimes and legislation for firms willing to export. GNIA also organises meetings, exhibitions and training seminars for managers and staff responsible for export sales. The web portal *www.tradewithgeorgia*.com was created by GNIA to increase awareness about Georgian products and to provide potential foreign buyers with comprehensive information. It contains a database of Georgian producers and a catalogue of Georgian products. Several contacts have already been established between Georgian and foreign companies. In addition, both GNIA and the Ministry of Agriculture of Georgia provide informational and financial support for participation in international trade fairs. There is no special support for SMEs and assistance is provided to all firms irrespective of their size.

The budget and human capacity of the GNIA is relatively limited. With a staff of only 23, GNIA has been given the mandate to undertake export promotion with only two additional staffing slots. In 2011, the budget was increased to USD 1.5 million, compared to approximately USD 500 000 *per annum* in previous years. However, the bulk of the new budget is dedicated to non-staff related promotional efforts. The agency is expected to undergo structural changes to both staff and organisation and is moving towards a more strategic approach to investment and export promotion. So far, a strategy does not exist, but the need to develop a relevant complex state programme for the purpose of encouraging export-orientated entrepreneurship is stated in the National Strategy for Regional Development 2010-17.

International organisations are also active in supporting Georgian SMEs that export. The German Chamber of Commerce organises free seminars on export promotion for firms. East Invest, a three-year programme which started in January 2011, promotes economic co-operation and facilitates investment between the European Union and the EaP countries, and among the EaP countries themselves. The project is expected to provide support to Georgian SMEs through training and coaching on the EU *acquis* and internationalisation, elaborating their sectoral strategies and investment mapping, participating in EU trade fairs, etc.

Single Market opportunities

In the context of the launch of negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU at the beginning of 2012, Georgia has made considerable progress in the area of addressing technical barriers to trade.

In 2011, the government submitted to parliament a Code on Safety and Free Movements of Goods. Furthermore, an institutional gap assessment was organised for regulatory bodies resulting in an Institutional Reform Plan. In 2010-11 Georgia became a corresponding member of the International Organization of Legal Metrology (IOLM), an affiliate member of CENELEC and an associate member of the International Electrotechnical Commission (IEC) and an associate member of the European Co-operation for Accreditation. Georgia is also member of the following international organisations in the field of standardisation – the International Organization for Standardization (IOS) (corresponding member from 2006), CEN (affiliated member from 2008)– BIPM (associate member from 2008) and the Euro-Asian Cooperation of National Metrological Institutions (COOMET) (member from 2006).In the area of sanitary and phytosanitary rules (SPS), Georgia started full implementation of its food strategy and also initiated legislation on SPS including the preparation of a framework law. The Food Safety Agency's statute was adopted and agency staff were trained with EU support.

SMEs are informed by the Georgian National Investment Agency (GNIA) on export conditions and opportunities for Georgian enterprises that are planning to engage in the EU.

The way forward

Based on the SBA assessment, Georgia could consider the following steps to ensure continuing progress in the area of SME development:

- Having successfully created a favourable operational environment for business activities, Georgia would benefit from consulting with the private sector to assess whether there is a need to develop and adopt an **SME strategy** that would identify strategic directions and objectives for future development of the SME sector, including for export promotion. Ideally, such a strategy would be based on a thorough assessment of the current performance of SMEs in the economy to identify policy barriers in those strategic sectors that have a high potential for SME growth. Such a strategy should also cover green economy elements.
- Similarly, the government could consider moving further towards evidence-based policy making by **systematically applying regulatory impact analysis (RIA)** to assess the positive or negative impact of regulatory changes on the SME sector. A major challenge that needs to be addressed in this process is to introduce a permanent consultative mechanism to assess and discuss implications of legislative proposals on SMEs. If appropriate, the results could be considered in the draft laws.
- Both the public administration and the private sector would benefit from an increased **scope of public-private consultations,** especially in priority sectors of the Georgian economy, such as agribusiness, light manufacturing and tourism. Although there are numerous business associations and an intensive network of chambers of commerce in Georgia, the capacity of associations in representing SME interests is limited.
- Export-oriented SMEs and SMEs with export potential would benefit from receiving updated, timely and **comprehensive information about export possibilities** and foreign market requirements. To strengthen the competitiveness of Georgian SMEs, it would also be important to further develop national quality infrastructure institutions and support their integration into the relevant international and EU institutions. International

recognition of Georgian conformity assessment results is essential for export-oriented SMEs, and will decrease the expenditures for companies carrying out export-related procedures.

- Ongoing **improvements in the legal and regulatory framework** would support further development of leasing activity as an alternative source of finance for SMEs. A more competitive banking sector will facilitate sustainable access to finance for SMEs. Better enforcement of creditors' rights to allow secured creditors to seize their collateral after re-organisation would help bank lending in general and SMEs in particular.
- The Georgian government has started to introduce sophisticated mechanisms such as technology transfer centres to strengthen the absorption capacities of SMEs for innovation and focus research outcomes on practical applications needed by the market. However, active policy measures are needed to increase **consultancy services and innovation support schemes** in Georgia. To make financing more available to SMEs, the private sector contribution to financing should be stimulated, thus creating more synergies between public-funded innovation and the needs of firms. The innovation process would also benefit from greater co-operation between universities, technological centres and industry in the innovation process. Developing a well-functioning innovation policy on the basis of the State Strategy on Regional Development 2010-17 would help to co-ordinate stakeholder activities and establish measurable objectives.
- Based on the important steps taken to enhance the quality of education and reinforce the entrepreneurial culture, Georgia could easily move forward to a **national lifelong entrepreneurial learning strategy** and optimise a systematic Training Needs Analysis (TNA). With a consolidated information system on training providers, this would lead to a more responsive training market and improved efficiency in training efforts to meet the evolving requirements of enterprises.

Notes

1. *http://transparency.ge/en/blog/pnew-regulations-concerning-tax-lien-explainedp*.
2. ISO 14000 requirements are an integral part of the EU's environmental management scheme (EMAS) and concern performance improvement, legal compliance and reporting duties.

Reference

EBRD (European Bank for Reconstruction and Development) (2009), *EBRD Insolvency Law Assessment Project – 2009*, EBRD.

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PART III

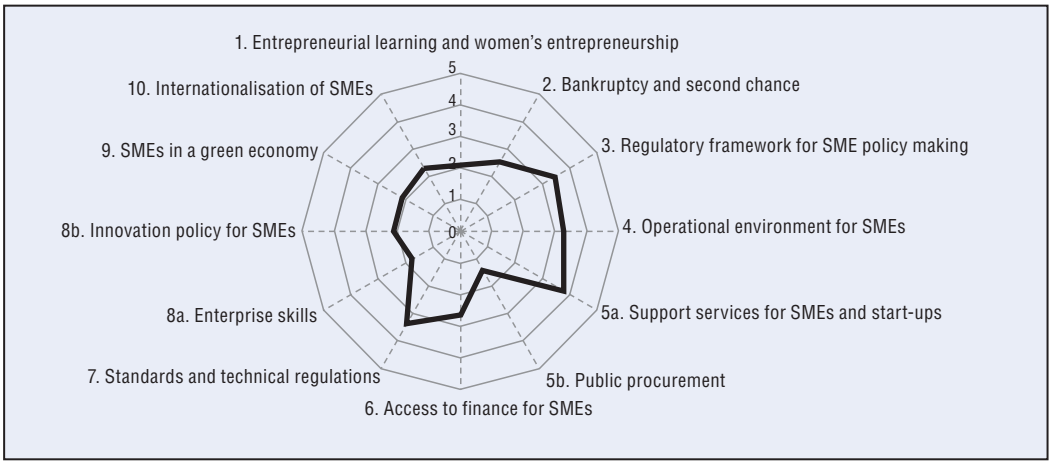
Chapter 17

SBA country profile: The Republic of Moldova*

A first round of evaluation of the SME policy based on the Small Business Act (SBA), conducted in 2010, showed a relatively developed institutional framework with important initiatives taken to simplify its legislative and administrative procedures. The current assessment shows some improvement in almost all indicators on registration procedures and e-government. The regulatory framework has been further simplified with the second stage of regulatory reform yet to be completed. A third stage, tackling permitted documents, started in 2011. While reforms are ongoing, addressing the needs of businesses already operating remains an important issue. Public-private dialogue rarely involves representatives from the SME community, and could strengthen their formal influence on the decision-making process. There is limited support for the provision and improvement of the quality of business services, and access to finance for SMEs remains a crucial issue.

* This chapter was prepared with the support of Business Intelligence Services and Sofia Suleanschi.

Figure 17.1. **SBA scores for the Republic of Moldova**



Note: The score for each dimension are calculated based on assigned weights for each indicator (see Annex A for further information).

Overview

This section provides a brief economic snapshot and highlights some recent trends in the business environment. This is followed by a detailed overview of the current situation of the SME sector in the Republic of Moldova.

Economic snapshot

The Republic of Moldova is a relatively small country, landlocked, and with limited natural resources apart from agricultural land. With a population of 3.6 million people, more than 20% of its population is working abroad, while domestically, the unemployment rate reached 6.4% in 2009.

The economic performance of the country is modest. With a GDP per capita of USD 1 631, it is the lowest in the Eastern Partner (EaP) region. Its economic growth is mainly based on the increased demand fuelled by remittances sent by workers abroad and trade based on basic agricultural and manufacturing products.

The Republic of Moldova is very open to trade. Its imports and exports together constitute 134% of GDP. Due to its dependence on external energy resources and imports sustained by incoming remittances, the country runs a high current account deficit.

During the crisis the economy was severely affected and its GDP contracted by 6%. The main shocks came from the outside, in particular the sudden reduction of remittances from over 30% of GDP in 2005-08 to 22.4% in 2009 and a slowdown of external trade which hampered economic growth. The country still remains vulnerable to external shocks due to its reliance on remittances and the prices of imported energy materials.

Business environment trends

Up to 2006, the Republic of Moldova performed poorly in cultivating the attractiveness of its business environment. Since then, the government has embarked on several reforms to address the most important issues, such as the simplification of its regulatory framework via the Legislative Guillotine and reduction of the tax burden. Over the past

Table 17.1. **Republic of Moldova: Main macroeconomic indicators, 2008-12**

Indicator	Unit of measurement	2008	2009	2010	2011	2012 (proj.)
GDP growth	Per cent, y-o-y	7.8	–6	7.1	6.4	4
CPI inflation	Per cent, average	12.8	0	7.4	7.2	4
Government balance	Per cent of GDP	–1	–6.3	–2.5	–2.4	–1
Current account balance	Per cent of GDP	–16.2	–8.6	–8.3	–10.6	–10
Net FDI	USD million	695	139	189	261	270
External debt	Per cent of GDP	55.2	65.5	67.3	67	72
Gross reserves	Per cent of GDP	27.6	27.4	31	30.3	31
Nominal GDP	USD billion	6.1	5.4	5.8	7	7.5

Source: EBRD (2011), data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks.

year the government of the Republic of Moldova has also undertaken further reforms in the areas of simplification of registration procedures and liberalisation of trade (EBRD, 2011).

SMEs in the Republic of Moldova

According to the Law on Support to Small and Medium Sized Enterprises, SMEs are defined according to three parameters: the number of employees, turnover and size of their balance sheet. The law identifies four categories of enterprises: micro, small, medium and large enterprises. A company is included in a category if it meets the related headcount ceiling and either the turnover or the balance sheet ceilings. The parameters for each category are described in Table 17.2.

Table 17.2. **Definition of micro, small and medium enterprises in the Republic of Moldova**

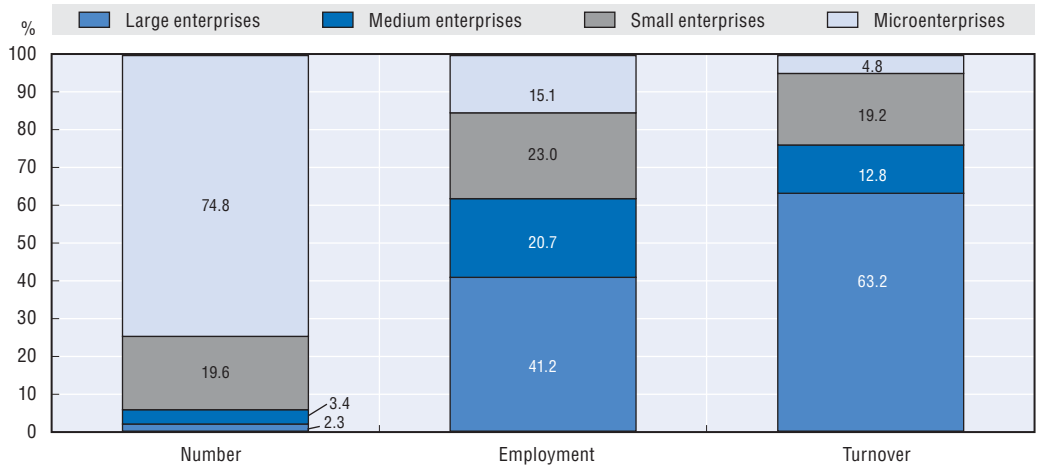
	Micro	Small	Medium	Large
Average numberof employees	< 10	< 50	< 100	Firms that are not included in the definition of micro, small or medium firms
Average annual revenues in MDL (EUR)	< MDL 3 million (EUR 182 000)	< MDL 25 million (EUR 1.5 million)	< MDL 50 million (EUR 3 million)	
Average annual; total assets	< MDL 3 million (EUR 182 000)	< MDL 25 million (EUR 1.5 million)	< MDL 50 million (EUR 3 million)	

Source: Law No. 206-VXI of July 2006 on supporting the SME sector, Republic of Moldova.

In 2010 there were 45 600 SMEs, which represented approximately 97.7% of the total number of enterprises based on the financial reports presented to the National Bureau of Statistics (NBS). These figures do not include microfirms that use a single-entry accounting system, patent holders or farmers, who represent an important proportion of microfirms. The number of SMEs has increased steadily since 2007 with an average annual growth rate of 4%.

Within the SME sector, the small enterprises have been the most dynamic. The number of active small enterprises increased by 27% over the period from 2007 to 2010 and employment rose by 8%. A positive but less marked increase was recorded in the microfirms – the number of microfirms increased by 15%. Employment in microfirms was 12% for the same period of time. This strong dynamic in the small enterprise and microsegments is partly compensated by the negative trends in the medium-sized segment. The number of medium-sized firms decreased in 2007-10 by 11% and

Figure 17.2. **SME sector in the Republic of Moldova, 2010**



Source: National Bureau of Statistics of the Republic of Moldova.

employment by 23%. This negative performance is mainly due to the financial crisis, which hit medium-sized firms particularly hard.

Employment in SMEs has steadily decreased since 2007, as it did in large firms but at a higher rate. As a result the share in employment of SMEs has gone down slightly and represented 59% in 2010.

While there is no actual figure for the contribution of SMEs to GDP by size, according to the NBS, SMEs overall contributed 28.3% to the GDP in 2010. The share of SMEs in turnover, on the other hand, is quite high (37%). This is specifically because micro and small firms are most active in the area of wholesale and retail trade, economic sectors that generate high turnovers. Microfirms in particular represent 78% of the firms operating in this sector.

SBA assessment results

This section outlines the main results for the Republic of Moldova from the 2012 SBA policy assessment in EaP countries and highlights the changes that occurred since the previous assessment in 2010. The assessed policy dimensions were reassembled and grouped under five wider SME policy areas.

Strengthening institutions and mechanisms for SME policy making

The development of SME policy in the Republic of Moldova is at a relatively early stage. However, there has been significant progress over the past years, and the main pillars for an institutionalised SME policy framework have been established.

Institutional framework

The SME policy is built around two main institutions: the Ministry of Economy, in charge of policy elaboration, legislative drafting and policy co-ordination and the Organization for SME Sector Development of the Republic of Moldova (ODIMM) acting as the implementation agency under the supervision of the Ministry of Economy. The legislative framework for SME policy is set by the Law on Support to Small and Medium Sized Enterprises which includes a comprehensive definition of SMEs, modelled on the EU definition, and provides guidelines for public policy in the area of SME development and support.

The Ministry of Economy is in charge of SME policy development, legislative drafting and policy co-ordination through the Directorate of SMEs and the liberal professions. SME policy forms a part of the government's overall economic strategy. In order to adopt a consistent approach, in February 2009 the government of the Republic of Moldova adopted a State Programme for Supporting SME Development covering the period from 2009 to 2011. This programme expired in 2011 and the new draft strategy to support small and medium-sized enterprises for the years 2012-20 and the action plan for its implementation are expected to be approved in 2012.

The task of SME policy implementation is assigned to ODIMM, founded in 2007, which acts as an executive agency under the supervision of the Ministry of Economy. The organisation aims to develop and implement programmes for small and medium-sized enterprises and its activity includes entrepreneurship promotion, service provision to SMEs and SME support in access to financing. Programmes developed by ODIMM include credit guarantees for micro and small entrepreneurs, matching grants for remittances invested in domestic companies, a number of business training programmes and the organisation of the annual SME Forum and International SME Conference, as well as thematic workshops, seminars and roundtables.

ODIMM receives funds from the state budget for the implementation of state programmes but is otherwise self-financed. It is a public not-for-profit, non-commercial institution and implements a number of business support activities. ODIMM presents its reports and annual budget for approval to a Steering Committee.[1] ODIMM works in close co-operation with its development partners: the Ministry of Economy, the 33 regional councils, the Moldovan Investment and Export Promotion Organization (MIEPO), the Chamber of Commerce and Industry (CCI), the Agency for Innovation and Technology Transfer (AITT), regional development agencies and business-related non-governmental organisations (NGOs) and associations. Nevertheless, because of the limited capacity of business associations to represent the interests of SMEs, ODIMM lacks an efficient mechanism for co-operation and consultation with the public and central and local authorities.

Legislative simplification and regulatory impact analysis (RIA)

The Ministry of Economy of the Republic of Moldova develops action plans to remove administrative constraints for businesses on an annual basis. The Working Group of the State Commission for Regulation of Entrepreneurial Activity meets on a weekly basis to review business-related legislation and regulations. During Guillotine I, the first stage of the regulatory review process held from 2005-06, 818 regulations were revised and 184 legislative acts were repealed. Guillotine II, the second stage of the regulatory guillotine process, was held from 2006-08 and involved the cancellation of 93 legislative acts. In 2010-11, a third stage of the guillotine was conducted (Guillotine II+), which reviewed over 400 permits issued by 43 public authorities, reducing their number to 273 and 34 respectively. In addition, a list of 270 papers were included as an annex to Law No. 160 from 22 July 2011 regulating the authorisation of entrepreneurial activity, which contains the type or category and size of payments that are to be charged for it. The final stage of the process (Guillotine III) is expected to review the list of paid services rendered to business by public authorities and the creation of a single register of paid services.

The legal framework and methodology for RIA is well established in the Republic of Moldova, and includes provisions for cost-benefit analysis and consideration of the rights

and interests of entrepreneurs for all draft business-related legislation. The Working Group of the State Commission for Regulation of Entrepreneurial Activity is responsible for RIA. In addition, the legal framework for RIA explicitly states that the final impact assessment should include an evaluation of the potential impact of the regulation on SMEs. The current SME strategy was developed without the implementation and impact analysis of the previous two strategies for the periods 2006-08 and 2009-11. For example, it is not clear what the major conclusions from the previous strategies are and how they were incorporated into the new strategy.

Public-private consultations (PPC)

Public-private dialogue in the Republic of Moldova is well established and regularly conducted within the framework of two main bodies: the Working Group of the State Commission for Regulation of Entrepreneurial activity and the National Participation Council. Despite the fact that neither of these bodies is dedicated specifically to SME issues, the dialogue generally covers the problems and legislation related to entrepreneurial activities and SMEs.

The main body for PPCs in the Republic of Moldova is the Working Group of the State Commission for Regulation of Entrepreneurial Activity. The core activity of the Working Group is RIA implementation but it also serves as a platform for public-private dialogue. The majority of topics discussed within the working group meetings concern regulatory reform, *e.g.* discussion of the changing needs of current legislation which regulates entrepreneurial activity (primary and secondary legislations).

The working group meets in ordinary session at least once a week. Its meetings are public and any limitation of access to its meetings is prohibited. The online transmission of its meetings can be accessed at *www.privesc.eu*. The calendar and agenda of the working group meetings for 2011 (but not 2012) is published on the Ministry of Economy website. The working group approves decisions by a majority of votes of the members present at the meeting. In case of parity, the document is considered as rejected, but the ultimate decision is made by the ministers during a government meeting. Separate opinions of members are included in the minutes on the meeting.

The National Participation Council (NPC), an institution headed by the Prime Minister, was established in 2010 and specifically aims to ensure the involvement of civil society in policy and decision making processes. The main functions of the NPC are participating in all stages of strategic planning and providing expertise in the areas of elaboration, evaluation and monitoring of public policies to public stakeholders. The NPC also facilitates public-private dialogue by monitoring the application of the Law on Transparency in the Decision-making Process, adopted in 2008, as well as by facilitating PPCs. The scope of the NPC assessment covers major policies that might have an impact both on particular sectors and/or organisations and covers a wider range of problems including SME issues. The NPC meets once every trimester and comprises 30 members of civil society organisations selected on a competition basis, with the possibility of including SME representatives.

Apart from the abovementioned platforms, there are also two advisory councils – the Advisory Council to the Ministry of Economy and the Economic Council under the Prime Minister – whose activities are also based on PPCs, but with more restricted access. Both councils invite pre-selected companies for PPCs, and there is no broad dissemination of coming council events.

Establishing a conducive operational environment

There has been considerable progress in the area of administrative simplification since the 2009 assessment. The main positive changes are the reduction of time and costs required to obtain a registration certificate as well as more possibilities to use online government services.

Company registration

The Republic of Moldova has achieved positive results in streamlining procedures for business registration. In particular, Article 5 of the Law on the State Registration of Legal Entities and Individual Entrepreneurs states that registration must be completed within 5 working days of the submission of all necessary documents to the State Registration Chamber. Moreover, for an additional fee, companies can obtain registration certificates within 24 hours or even within 4 hours. The three steps required for obtaining a company registration certificate can all be carried out at the one-stop-shop in the State Registration Chamber.

In the Republic of Moldova, the State Chamber of Registration has established one-stop-shops under the Decision on Several Measures for improving the enterprises and organisations state registration system, dated 20 December 2001. However, one-stop-shops do not allow for all necessary registration and notification procedures to be completed at the same location. According to the World Bank's *Doing Business 2012* report, start-ups are still required to register with the State Registration Chamber, the Ministry of Information Technologies and Communication (included in the registration process), the Territorial State Fiscal Inspectorate, the Social Security Fund and the National Medical Insurance Company. The State Registration Chamber has also established a pilot project for online registration, which allows entrepreneurs to reserve a company name, download model registration forms, submit the necessary documents for registration and obtain a company registration certificate online.

In the Republic of Moldova, the silence-is-consent principle is included in Article 11 of the Law on the Regulation of Entrepreneurial Activity dated 20 July 2006, and Article 2 of the Law on Licensing of Entrepreneurial Activity dated 30 July 2001, for the issuing of general licences and permits to initiate and conduct business. The principle of "tacit approval" is also included in Article 16 of the Law on the Regulation of Entrepreneurial Activity dated 20 July 2006, as a general principle for adoption by all government institutions involved in regulatory activities. However, the silence-is-consent principle is currently not included in the law on registration.

Interaction with government services (e-government)

Online filing of tax returns and social security contributions is envisaged under the National Strategy for Information Society – Electronic Moldova (2005) and Judgment No. 733 On the Concept of Electronic Government (2006). In July 2009, the State Tax Inspectorate under the Ministry of Finance launched a pilot project for electronic reporting of tax returns, with the assistance of UNDP and USAID's Business Regulatory and Tax Administration Reform Project (BIZTAR). The system is still not fully developed, and does not allow for credit and debit compensation to be conducted online. The development of a range of e-government services including online filing of social security returns, electronic procurement and customs declaration is envisaged under the action plan for the National

Strategy for Information Society – Electronic Moldova. Implementation of the measures envisaged under the action plan will permit increased online communication between SMEs and government institutions.

The Law on Electronic Documents and Digital Signatures was adopted in July 2004. It includes measures to allow for the official accreditation of electronic signatures. The UNDP project Implementing e-governance is working to revise the current legal framework for electronic signature in order to further simplify procedures and reduce costs for applicants. At present, e-signature is available for electronic filing of tax returns with the State Tax Inspectorate.

The government has developed a plan to create an automated information system, allowing for full connectivity between the databases of government ministries and the National Bureau of Statistics. The plan was approved in September 2010, and implementation is expected to proceed in the near future. The government has also attempted to integrate the database of the State Registration Chamber with numerous other government institutions (Ministry of Information Technologies and Communication, the Territorial State Fiscal Inspectorate, the National Social Security Fund, the National Medical Insurance Company, etc.) However, connections are not properly established and do not allow for data viewing across institutions. As a result, entrepreneurs are still required to register with these authorities separately.

Bankruptcy procedures and second chance

Laws and regulations on bankruptcy procedures are established through the Insolvency Law enacted in 2001, and its subsequent amendments. The law distinguishes three forms of insolvency procedures: foreclosure, liquidation and re-organisation. It has been subject to a number of modifications since it entered into force and is considered to be in line with international standards. Indeed, an assessment of the insolvency framework carried out by the EBRD in 2009 concluded that compliance with international standards was medium (EBRD, 2009).

The law clearly sets out the criteria for commencing proceedings and preventing pre-bankruptcy transactions. Once the insolvency procedure is initiated, a provisional administrator is nominated by the court which will oversee the insolvency procedure and, if needed, liquidate the company. In practice, however, the situation appears to be more difficult. In the World Bank's *Doing Business 2012* report, the Republic of Moldova ranks 91st (out of 183 economies) on the Resolving Insolvency indicator. In particular, the time required to complete a bankruptcy is 2.8 years, costs incurred through the proceedings are 9% of the estate's value and the recovery rate for creditors is 31.3 cents on the dollar (the OECD average is 69.1 cents on the dollar).

In order to improve the efficiency of the insolvency process, reforms should be taken to reduce delays in the procedure. Measures may also be taken to ensure that the officials in charge of administrating insolvency procedures have received sufficient training. In particular, ensuring that insolvency administrators have an adequate level of competence is central to the proper functioning of the insolvency framework. The specialised economic courts dealing with bankruptcy cases were liquidated in July 2011 (a final decision is still pending with the Constitutional Court).

The public administration could play a more supportive role regarding second chance treatment. Even though there are no discriminatory measures which would restrict access

of re-starters to business support schemes or public procurement tenders, regulations for discharge and debt settlement are disadvantageous. Discharge procedures are not determined by law. This enables creditors after cessation of insolvency proceedings to freely pursue an individual debtor without limitation. Regarding debt settlement, tax debts take first priority over any other debt in a bankruptcy which puts secured creditors in an unfavourable position.

Facilitating SME access to finance and developing a legal and business environment

Similarly to other countries in the region, lending to SMEs is mainly provided by banks and a number of microfinance organisations. Public financial support is limited. Other sources of finance such as leasing are not enough or fully developed to represent an alternative source of finance and the availability of private equity is very limited. A fully functioning cadastre and a central collateral registry are in place. The coverage of the recently established private credit bureau is low. Recent improvements in creditors' rights legislation are positive, although not sufficient to ensure the seizing of collateral.

Sources of external finance for SMEs

Domestic credit to GDP was about 36% in 2011 and lending to SMEs is estimated to be about 31% of banks' loan portfolios. Nevertheless, a significant share of SMEs perceives access to finance as a major obstacle, in particular the availability of long-term loans for investment purposes. Banks have only limited external funding, mostly from international finance institutions (IFI) and parent banks in the case of foreign-owned banks. The international financial crisis has had a significant negative impact on bank lending, including a sharp drop in remittances, mainly in 2009. Lending growth has recovered recently to 16% in 2011 from a drop of 8% in 2009.

The public Credit Guarantee Fund created in 2004 is operated by the Organization for SME Sector Development (ODIMM) with its main focus on rural areas. It offers four different credit guarantee products targeting diverse groups such as active enterprises or young entrepreneurs, and it currently collaborates with four commercial banks. A private credit guarantee fund set up in 2006 is run by GarantInvest, created by seven local commercial banks, one microfinance organisation and one public association. These two guarantee schemes are underused, both because their activities are quite recent and because the rate of coverage seems to be too low (50% of the loan amount).

The guarantee fund operated by ODIMM also guarantees 70% of the loan amount for rural start-ups. These state programmes implemented by ODIMM to promote start-ups also include the National Programme for Youth Economic Empowerment (NPYEE), the Pilot Programme for Attracting Remittances into the Economy (PARE 1 + 1) of around MDL 15 million and the Credit Guarantee Fund (FGC).

The microfinance sector is represented by 53 microfinance institutions (MFI) representing total assets of MDL 2 billion (USD 169 million) and 396 savings and loan associations (SLA) representing MDL 386 million (USD 33 million) operating since 1998. Nevertheless, the microfinance sector continues to cover a limited part of SMEs' needs. The activities of the MFIs and SLAs are regulated by the National Commission of Financial Market (CNPF). The market is poorly monitored, however, due to insufficient capacity at the CNPF.

The leasing market is regulated by the Law on Leasing which was adopted in 2005. The law clearly defines various aspects of leasing contracts as well as the obligations of the parties. Currently 27 leasing companies operate in the country. They have been established

mostly by banks and some leasing firms are owned by foreign strategic investors. The top three companies control 50% of the leasing market. However, the volume of transactions remains very low and is mostly confined to car leasing. The CNPF is responsible for monitoring the leasing market.

Availability of risk capital is limited. Some foreign venture capital funds operate in the country but there is no national fund. Despite some civil society initiatives to draft a law on venture capital, there is no legal framework.

The Moldovan Stock Exchange (MSE) is in place and its supervision has improved since 2007 when CNPF replaced the National Securities Commission as a supervisor. MSE is a closed-end joint stock company where members must be shareholders, must be licensed as broker-dealers for market activities, and have to comply with requirements on solvency, organisation of operations and employees. Despite a good legal framework in place, access to the stock market for SMEs is limited. While the government bond market is relatively developed, the public equity market is not, with a stock market capitalisation equal to 20.4% of GDP at the end of 2010.

Legal and regulatory environment

A functioning cadastre registry is in place. The territory of the Republic of Moldova is currently fully registered and the cadastre information is available online. In 2010, the number of procedures to register a property was simplified and the time required was considerably reduced. On September 2008, a new law, the Law on Mortgage, entered into force. The main goal of the reform was to consolidate a single law all provisions concerning mortgage, which had often resulted in contradictory, unclear and incomplete provisions.

The private Credit History Bureau LLC (CHB) was founded in 2008, following the adoption of the Law on Credit History Bureaus. The CHB obtained its licence from the National Commission of Financial Market in 2010, and launched its activity in April 2011. The current participants in the CHB are 14 Moldovan commercial banks, two leasing companies and one Romanian private company. Access to the data is available to the subjects of the credit information once per year without charge and as many times as required for a fee. The historical data available is maintained for a maximum of seven years. Nevertheless, given its recent establishment, information coverage is currently low, with only 3% of adults being reached.

A central collateral registry is in place, unified geographically and by asset type. However, an online system for registration of movable assets is not yet available. Companies may use movable assets as collateral depending on their value and the type of the loan or agreement being requested.

Lending is largely collateralised by real estate and collateral requirements remain high. Nevertheless, commercial banks currently provide credit up to MDL 30 000 (consumer loans) and MDL 100 0000 (business loans) without any collateral required. Commercial banks must make provision for at least 5% of the loan amount with respect to such uncollateralised credit.

Creditor rights are addressed in the Law on Collateral, the Law on Insolvency, the Law on Financial Institutions and the Enforcement Code. Amendments to existing legislation, made in 2010, have enhanced creditor rights in protecting their interests for the recovery of bad loans and an enhanced enforcement of guarantees. The law allows both for liquidation and re-organisation of insolvent companies. Overall, the procedures are well defined;

secured creditors are paid first out of the proceeds of liquidation of a bankrupt firm. Nevertheless some improvements could be made on re-organisation procedures, such as guaranteeing secured creditors the right to seize their collateral after re-organisation. Re-organisation is nevertheless not often used; liquidation and foreclosure seem to be the preferred option.

Other factors that affect demand and supply of finance

The financial literacy level in the Republic of Moldova is low amongst companies and there is a certain lack of trust in the financial sector. The Moldovan government is therefore funding training and information programmes, implemented by ODIMM. ODIMM carries out information campaigns among entrepreneurs throughout the country and organises workshops and conferences on financial products for SMEs. Some commercial banks have also developed programmes and seminars to enhance the existing level of knowledge in financial services. EBRD BAS, USAID and some commercial banks have also developed programmes and seminars to enhance the level of knowledge in financial services. However, a national strategy on financial literacy does not exist and there is little co-ordination among the various initiatives.

Promoting a culture of entrepreneurship and skills development

A new strategy and action plan initiative for the development of SMEs is embedded in the National Development Strategy 2012-20 (Moldova 2020). It will also contribute towards the coherence and involvement of stakeholders in the field of entrepreneurial learning (EL) and the development of enterprise skills.

At this stage policy partnership and policy dialogue in relation to EL are ongoing but unstructured along the different policy initiatives. Evidence shows that the conditions for institutionalising dialogue are present. Such conditions can also bring coherence to the policies and involve stakeholders more actively. The plan to develop a National Qualifications Framework (NQF) may also stimulate policy partnerships if a range of stakeholders is involved throughout the process.

The National SME Strategy has a component on Entrepreneurship and Human Capital Development that aims at creating a diffused entrepreneurial culture across the country, a culture that values learning, initiative and creativity at any stage of people's lives.

At present, although there are a number of good practices, the conditions are not favourable for the exchange of such good practice. This is due to the weakness of educational networks with regard to EL and not-so-easy access to information sources.

The non-formal offer requires attention and would benefit from more transparency. Although many different initiatives are in place, the tools for quality control are not as developed. If quality assured recognition of non-formal and informal learning could be implemented, it would help to create progress and transparency at the same time.

A 72-hour module is envisaged by the Ministry of Education to ensure the presence of entrepreneurship in the education plan at the ISCED 3 level. The implementation of the module is voluntary, and the result depends very much on each school and teacher. Some sources describe the module as theoretical and loosely linked to real situations. They are doubtful about the nature and effectiveness of this module especially within the context of vocational education and training curricula. The Ministry of Education has acknowledged the weakness and has asked experts to review the content of the 72 hours of the module.

The recommendation is to treat entrepreneurship as a core competence to be taught in education starting at the lower levels, to prepare future entrepreneurs as well as people capable of taking initiatives and implement them as employees or independent workers.

With regard to women's entrepreneurship, a policy framework is expressed by the National Programme on Gender Equality for 2010-15, which is developed and should be implemented. In the national state program on support of SME development 2009-11. Specific reference is made to the promotion of women's entrepreneurship. The figures in the state programmes PNEAT, Pare1+1 and GEA demonstrate the presence of an average of 35% participation by women. The women's economic empowerment programme (WEE) is an initative to inform and actively involve women from both rural and suburban areas in these state-supported programmes. Effective monitoring would support ongoing improvements, with a view to making the policies on women's entrepreneurship more effective. This is a challenge.

Although there is awareness of the relevance of an agreed national system of training needs analysis (TNA), there is no framework for it. The new National Strategy on SMEs indicates this in the component on Entrepreneurship and Human Capital Development. Good practice is well illustrated by the work of two sector committees and experts who have conducted training needs analyses, and further developed first occupational standards on that basis. Stakeholders, such as sectoral social partners, the chamber of commerce and donors in the Republic of Moldova undertake surveys in order to identify training needs when required. The challenge is to systematise the approach and regularly put in place recognised mechanisms to feed the analysed needs into education training and other relevant forms of learning. The analyses should include the various needs in competence and skills, theory and practice, for both lower and higher levels.

Private-public co-operation between the ministries of economy, employment, education and social partners and other relevant private stakeholders should be part of this mechanism.

ODIMM carries out training for enterprises. The website co-ordinated by ODIMM provides information about the existing offer from different, mainly non-formal, training providers, and not only in Chisinau. With this excellent foundation, more detail is recommended for the future. It should include content and the expected outputs of the proposed courses, advice for different categories of participants and other relevant information. Access is sometimes impeded by the restrictions imposed on courses, or by a lack of funding, or a lack of awareness about the usefulness of learning. Co-ordination between different programmes and between the offers of different institutions (*e.g.* the employment services, other stakeholders, donors) would be an advantage. These recommendations, among others, were formulated during and after the workshops that contributed to the action plan for SME development.

So far, there is no national framework for quality assurance (QA) in the Republic of Moldova, either for formal or for non-formal training of SME's.

Quality assurance is carried out on an *ad hoc* basis within the initiatives of the different stakeholders. Current policy developments, including the SMEs strategy and the plan for a future NQF will make the development of a national framework for quality assurance indispensable. The quality of training both informally and formally, as well the identification of the relevant qualification standards will be crucial to the implementation of a quality system.

The OECD-ETF workshop explicitly highlighted relevance, the quality of trainers, awareness of policymakers in regard to quality and the importance of skill-based education and training.

Measures and services for start-ups and enterprise growth are supported by a number of programmes. Data show a certain degree of success among young entrepreneurs, returning migrants and start-ups. Focused follow-up may contribute to greater success rates and sustainability.

Enhancing SME competitiveness

The business support infrastructure of the Republic of Moldova is underdeveloped and, apart from a few donor-funded programmes, SMEs and start-ups do not have access to a wide range of business services.

Business information and services

At the moment there is no government action plan on improving the market for business services. The new SME Development Strategy for 2012-20 stipulates the development of a network of authorised business providers through the adoption of a quality system, increasing the level of their professional training and stimulating demand for business services among SMEs. A similar measure for development of business services was stipulated in the State Programme for SME development for 2009-11, but was not fully implemented.

In the Republic of Moldova, business services are available through a combination of public-funded and private business providers; 175 companies provide business services, including government organisations, private companies and NGOs and projects financed by foreign partners, associations, chambers of commerce, etc. Even though business services are provided by a wide network of private and public-funded business services providers, the demand for business services from SMEs is low, due to a lack of trust and no guarantees that the services will be relevant for their business. In order to assure clients of their quality, several business providers are applying for certification from TAM/BAS, which provides an internal system for accreditation of business services for participants in the programme. However, on a national level there are no mandatory quality standards for business services. The creation of a quality system is envisaged in the Action Plan for 2012-14.

Business information is available on the centralised portal for SMEs (*www.businessportal.md*). It is also available in English. It has a multiple search engine for more efficient navigation, and a special section for business-related discussions and questions. More fragmented information on the availability of business services can be found in some local offices.

Support for non-technological business start-ups is a separate component of donor-funded projects, such as Efficient Business Management and Simple Accounting, co-ordinated by ODIMM. There is no centralised action plan on start-up support and the draft document, Strategy to Support the Small and Medium sector for 2012-20 does not include any provisions for start-ups. Advisory support services for start-ups are only available in some donor funded projects (*e.g.* TAM/BAS).

In the Republic of Moldova there are a number of incubators. Among them are Entrepreneurship House (Ungheni), which offers 32 rooms furnished with appropriate offices to help prospective or current entrepreneurs to start or grow their business, as well

as ELIRI-INC (Chisinau), ASEM (Chisinau) and Impulse (Balti). The business incubator in Soroca is the first incubator in the Republic of Moldova with a mixed profile, which provides small entrepreneurs with both manufacturing facilities and office space. Currently, 17 companies are being incubated, of which 50% are start-ups. However, there is no strategy on incubators, although one is currently under discussion. Local initiatives are also in preparation.

Public procurement

It is not specified whether the Law on Public Procurement allows for cutting tenders into lots. No information is provided on the setting of proportionate qualification levels and financial requirements or on the possibility of joint bidding. The law does not discriminate against foreign operators. Late payments are not challenged via a separate legislative framework.

Information on Public Procurement is centralised at national level on the procurement portal (*www.tender.gov.md*) but the consultation of tender documents is not free of charge; consulting services are offered by the Public Procurement Agency and e-procurement solutions are in their testing phase.

Innovation policy

According to the Code on Science and Innovation, the Academy of Sciences of Moldova is responsible for the co-ordination of activities related to science and innovation. The implementation of state policy for innovation and technology transfer is conducted by the Agency for Innovation and Technology Transfer (AITT). The AITT also works to create links between the private sector and public research institutions.

The Code on Science and Innovation includes strategic objectives and directions for the development of innovation policy in the Republic of Moldova. Innovation policy is also covered in a number of other strategic documents, such as the National Development Strategy for 2008-11 and the State Program for Supporting SMEs (2009-11). Further co-operation on innovation policy may be achieved through the approval of the 2012-20 National Strategy for Innovation which is currently in draft form. The strategy will include policy measures and projects to promote innovation and encourage increased co-operation between the private sector, government, research institutions and universities.

There are three publicly funded science and technology parks operating in the Republic of Moldova: Academica, which is generalist, INAGRO, which focuses on agriculture, and Micronanotech, which specialises in nanotechnology. In addition, the Technological Transfer Network of the Republic of Moldova works to promote innovation and technology transfer at the national level, by creating a platform for interaction between research centres and other key stakeholders. Participation by the public sector and universities in innovation-related activities is poor, as there is no established structure or platform and access to public funding in the field of innovation is limited.

SMEs in the Republic of Moldova have limited access to consultancy and business planning services. As a result, companies are often forced to rely on donor-funded technical assistance programmes (*e.g.* EBRD's TAM/BAS, EU-funded programmes) There are also a number of pilot projects in place to provide funding and specialised support for innovative SMEs. For instance, the AITT uses approximately 70% of its budget to provide direct subsidies for companies to develop products based on new and innovative research

conducted by public institutions. In addition, ODIMM supports innovative SMEs by providing microfinance, loan packages and credit guarantees.

Green economy

The Moldovan government does not provide any reference in its policy framework to eco-efficient business and eco-innovation.

Although a number of organisations propose and implement projects on energy efficiency and other environmental issues, it is often not clear if these projects are addressed to SMEs.

The Moldovan government does not promote the use of environmental management systems or standards. Companies in the Republic Moldova decide on their own behalf to adopt and apply these systems if they are willing to correspond to market requirements or have strong principles of social responsibility.

Export promotion

The Strategy of Attracting Investments and Promoting Exports for 2006-15, on the one hand sets the strategic directions for export development for 2006-15, and on the other hand provides an action plan for achieving its objectives. MIEPO, the agency working under the Ministry of Economy is responsible for export promotion activities and implementation of this strategy.

A number of events are organised to promote entrepreneurship and support SMEs in promoting their products both on the internal and external markets. For example, ODIMM organises the Made in Moldova exhibition, the contest Best Entrepreneur of the Year, and the National SME Forum which combines a conference, consultations, seminars and a competition for SMEs and SME stakeholders. MIEPO also organises events for specific sectors (seminars on export of fruit and vegetables to the German market, Fashion trends 2010-11). SMEs are generally aware of the big promotion events organised by MIEPO. However, they rarely use the other services offered by the agency. In addition, MIEPO supports the participation of local producers in international exhibitions, such as the International Exhibition of Inventions in Geneva and the presentation of local wines at international wine festivals.

A lack of financial resources for the implementation of the abovementioned strategy remains an issue. The formulation of the financing element within the document is very general, making a vague link to the national budget, with no concrete financial provision specified for the export programme. Moreover, its funds are mainly absorbed by its promotional events and little remains for other activities related to export promotion. The effectiveness of these events is not clear, as the agency does not gather any statistics.

Single Market opportunities

In the context of the launch of negotiations on a Deep and Comprehensive Free Trade Agreement (DCFTA) with the EU at the beginning of 2012, the Republic of Moldova has made substantial progress in the elimination of technical barriers to trade.

A number of international and European standards have been adopted, New Approach Directives[2] have been transposed into national law and conflicting national standards have been withdrawn. The Republic of Moldova has made some progress in the affiliation process to the European Committee for Electrotechnical Standardization (CENELEC) and became an affiliated member of the International Electrotechnical Commission (IEC) in 2011.

In addition, amendments to the Law on Standardisation, a draft Law on Accreditation and Conformity Assessments Activity and amendments to the Law on Metrology have been submitted to parliament by the government.

The Republic of Moldova also continued to work on achieving closer alignment with EU sanitary and phytosanitary standards (SPS). In 2011, a food strategy for the years 2011-15 was adopted including the establishment of a food safety authority and plans for approximation with EU standards. Legislation on SPS border controls was also adopted. Finally, there is a need for the Republic of Moldova to fully implement its food safety strategy.

SMEs are informed by MIEPO and the Enterprise Europe Network (EEN) on export conditions and opportunities for Moldovan enterprises planning to engage in the EU.

The way forward

Based on the SBA assessment, the Republic of Moldova could consider the following steps to ensure continuing progress in the area of SME development:

- After conducting an extensive legislative review and simplification, and setting the institutional building blocks for SME policy, the Republic of Moldova would benefit from adopting the **strategy for SME development** which is currently being developed. The adoption of the strategy should be further complemented with monitoring mechanisms and tools for assessing the effectiveness of the measures undertaken. It is recommended to include green economy elements in the SME strategy.
- **Improvements in transparency and corporate governance, competition, and greater sophistication in the banking sector** while ensuring macroeconomic stability will facilitate sustainable access to finance to SMEs. The drafting of risk capital legislation and further improvements to the business environment (related also to increased investment and exit prospects) would support growth of private equity capital. Further improvements in information dissemination and greater accessibility of private credit bureaus, as well as ensuring creditors' rights to allow secured creditors to seize their collateral after re-organisation would support bank lending for SMEs.
- A framework that ensures **ongoing co-operation on innovation between government, academia and the private sector** could be established to ensure the practicality and efficiency of the innovation process. A shift to a private-sector driven innovation process is encouraged, but with financial and technical support from the public sector and academia.
- Export promotion could be given more consideration, in particular through **more targeted services for SMEs with the capacity to develop export capabilities**. Services could include the provision of information on export possibilities and creation of contacts and links between local firms and potential international business partners. Providing sufficient resources for export promotion activities remains a major issue.
- The creation of a widespread entrepreneurial culture should be supported by **effective education and training**, with a view to sustaining the success of SMEs policies in the long-term.

Notes

1. The Steering Committee is composed of the Minister of Economy, Vice-president of Chamber of Commerce and Industry of Moldova, Head of the Directorate SME Development of Ministry of Economy, Head of Monitoring and Analysis Directorate of the Ministry of Finance, the President of the Alliance of Associations for SME development, the Director of EBRD Moldova and the Director of ODIMM.
2. New Approach Directives are a series of measures to simplify the movement of goods throughout the European Union (EU) and the European Free Trade Area (EFTA). New Approach Directives provide controls on product design and above all, seek to harmonise product safety requirements across Europe.

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PART III

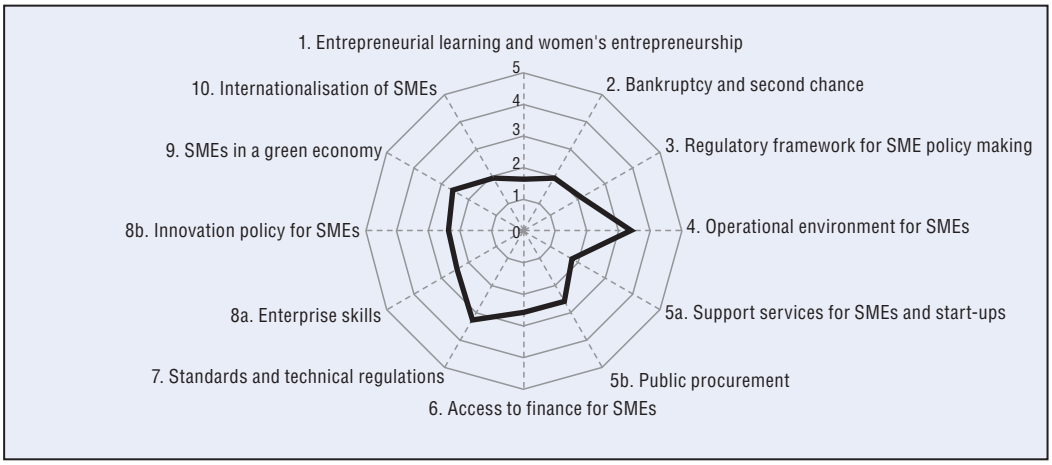
Chapter 18

SBA country profile: Ukraine*

Ukraine's commitments to SME development show some progress in deregulation and simplification of administrative procedures, but there is still room for improvement. The overall business environment continues to deteriorate and there is no coherent approach to SME policy making, no efficient strategy, policy tools or resources. Directives remain on paper and without implementation. Lifelong entrepreneurial learning will require greater engagement of all stakeholders working in partnership, particularly to address entrepreneurship as a key competence at all levels of education. Improved intelligence on enterprise skills will be critical to policy making and allocation of resources for training. Women's entrepreneurship requires better policy, follow-up actions and more advocacy. Important initiatives taken in innovation policy, access to finance and SME support tools have seldom been enforced. The institutional framework for SME policy making needs strengthening and support with public-private dialogue and monitoring tools as well as provision of business services and export promotion.

* This chapter was prepared with the support of Alexander Tsepko.

Figure 18.1. **SBA scores for Ukraine**



Note: The scores for each dimension are calculated based on assigned weights for each indicator (see Annex A for further information).

Overview

This section provides a brief economic snapshot and highlights some recent trends in the business environment. This is followed by a detailed overview of the current situation of the SME sector in Ukraine.

Economic snapshot

Ukraine is the largest country in the Eastern Partner (EaP) group of countries, with an area of 603.5 thousand sq. km and a population of 45.8 million people (68.7% in urban areas). The country has a high unemployment rate (8.1% of the labour force[1]) and the proportion of wages to GDP is still small. This is mainly a result of economic concentration on processing of raw materials rather than developing high-value-added finished goods. Productivity is low compared to more advanced economies, and the country's comparative advantage is based on its cheap labour force (EBRD, 2011).

Industry and agriculture, the main export-oriented sectors of Ukraine's economy, represent 41.2% and 7.7% of GDP respectively (Ukrstat). Services remain the largest sector, accounting for 45.8% of GDP (Ukrstat).

Ukraine is less dependent on energy imports than other EaP countries. Exports are mainly low-value-added non-precious metals (28.4% of exports in 2010), in particular steel and mineral products (13.1%).[2] In 2009, Ukraine was also the seventh largest exporter of wheat in the world (FAO). The country has attracted large amounts of foreign direct investment (FDI) in energy-intensive sectors, particularly in the areas of mining and quarrying. This is mainly due to its competitive gas prices.

Due to its reliance on foreign borrowing and commodity prices (particularly steel), Ukraine was severely hit by the crisis in 2008-09. During this period annual inflation reached 20%. The country's recovery continues to be hindered by a weak government response to the crisis and an uncertain external environment.

Table 18.1. **Ukraine: Main macroeconomic indicators, 2008-12**

Indicator	Unit of measurement	2008	2009	2010	2011	2012 (proj.)
GDP growth	Per cent, y-o-y	2.3	–14.8	4.2	5	2.5
CPI inflation	Per cent, average	25.2	15.9	9.4	7.7	6
Government balance	Per cent of GDP	–3.2	–11.3	–9.9	–4	–3
Current account balance	Per cent of GDP	–7.1	–1.5	–2.9	–3.9	–5.3
Net FDI	USD million	9 903	4 654	5 759	6 300	7 100
External debt	Per cent of GDP	56.4	88.2	85.1	76.2	73.2
Gross reserves	Per cent of GDP	17.1	21.8	25	22	22
Nominal GDP	USD billion	180.1	117.2	137.9	162.9	184.9

Source: EBRD (2011), data collected from *World Economic Outlook* (IMF), World Bank, National Statistical Agencies and Central Banks.

Business environment trends

In 2010-11, the government undertook a number of measures to improve the business environment, such as the adoption of a new anti-corruption law and the optimisation of government work by cutting the number of executive bodies. In addition, a number of other laws were adopted that reduce regulation in the areas of construction permits, VAT refunds and taxation.

Even though progress has been achieved in alleviating the tax burden and speeding up registration and licensing, the overall business environment is still perceived as rather unfavourable. Adopted reforms are often not implemented and remain on paper. Also, limited involvement of the private sector in the process of policy design and consultation remains an unresolved issue. As an example, the newly adopted Tax Code (as of 1 January 2011), which is intended to streamline the complicated tax system and reduce corporate income tax, is seen as highly controversial and is considered to pose a serious threat to small businesses. Moreover, economic activity in Ukraine remains highly concentrated in the hands of a limited number of people, often with political links.

SMEs in Ukraine

The statistical data on SMEs is based on the old definition for small and medium-sized entrepreneurship set by the Commercial Code of Ukraine. There is no definition for microenterprises which has become an obstacle to the efficient allocation of already limited state support for the SME sector. Individual entrepreneurs, who account for about 84% of the total number of registered and active business entities in Ukraine and employ 26.1% of people (including the owners), are also not included in the definition of the SME sector.[3]

Even though the share of SMEs in the total business population of legal entities was stable at around 99.5% for the last four years, both employment and turnover in the sector has been significantly reduced. Employment decreased particularly in medium-sized enterprises, approximately 10% each year between 2007 and 2010. The SME sector currently accounts for 58.1% of total employment (small – 26.3%; medium – 31.8%). In terms of turnover, the share of the SME sector has dropped from 60.7% in 2007 to 51.2% in 2010. These downward trends across all main indicators suggest that the SME sector is in need of more enabling policies to foster SME competitiveness.

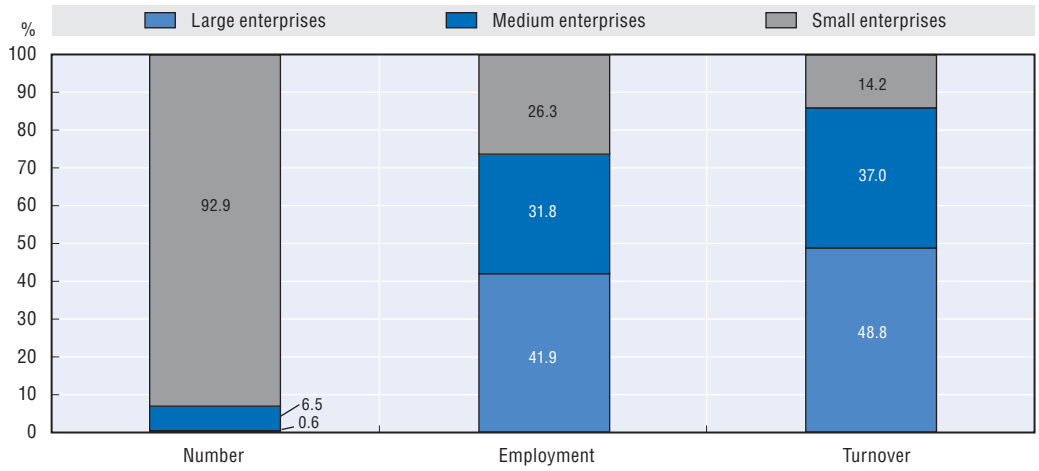
Statistical data on the number of small, medium and large-sized enterprises and the distribution of SMEs across different sectors and regions (not within one sector) are scarce.

Table 18.2. **Definition of micro, small and medium enterprises in Ukraine**

	Micro	Small	Medium	Large
Old definition				
Headcount	≤ 50		All enterprises that do not fall into the category of small or large enterprises	≥ 250
Annual turnover	≤ UAH 70 m (EUR 6.3m)			≥ UAH 100 m (EUR 9.1 m)
New definition				
Headcount	≤ 10	≤ 50	All enterprises that do not fall into the category of micro, small or large enterprises	≥ 250
Annual turnover	≤ EUR 2 m	≤ EUR 10 m		≥ EUR 50 m

Source: Commercial Code of Ukraine of 16 January 2003, No. 436-IV, Article 63; Law of Ukraine, No. 4618-VI from 22 March 2012 on State Support of Small and Medium Entrepreneurship in Ukraine.

Figure 18.2. **SME sector[1] in Ukraine, 2010**



1. Individual entrepreneurs are not included.

Source: State Committee of Ukraine for Statistics.

Based on the available information, sectors with a large share of SMEs (*versus* large companies) are real estate operations, rent, engineering, provision of business services (96.3%), construction (95.6%) and hotels and restaurants (95.3%).[4] Agriculture, hunting and forestry and industry sectors have a large proportion of medium-sized firms (20.4% and 11.7% respectively).

Small enterprises are concentrated in large cities (Kyiv and Sevastopol) and in several other regions with important urban centres. Among them are Kharkiv with 76 small firms per 10 000 inhabitants; Lviv with 70 and Kyiv with 65. The highest concentration of medium-sized firms is in large cities, particularly in Kyiv and Kyiv Oblast (Province of Kyiv).

The complex nature of business regulation has led to many businesses still operating informally, and which are therefore not accounted for in official statistical data. Even though there are no official numbers for the size of the informal sector, informal employment is estimated at about 4.5 million people between the ages of 15 and 70, or 22.1% of total employment. The majority (61%) of those informally employed are working in micro and small-sized enterprises. In terms of economic activity, informality is most relevant in private agricultural production units, including unpaid family workers (90.1%) and construction (39.4%) (World Bank, 2011).

SBA assessment results

This section outlines the main results for Ukraine from the 2011 SBA policy assessment of EaP countries. The assessed policy dimensions were reassembled and grouped under five wider SME policy areas.

Strengthening institutions and mechanisms for SME policy making

The SME support policy priorities in Ukraine are outlined in the Law of Ukraine on State Support of Small and Medium Entrepreneurship in Ukraine adopted in March 2012. The institutional framework for SME policy is in the process of being restructured.

Institutional framework

The roles of the government bodies involved in the support of SME development are set by the Law of Ukraine on State Support of Small and Medium Entrepreneurship in Ukraine, adopted in March 2012. The Cabinet of Ministers develops the state programmes for SME support and co-ordinates the executive bodies involved in the implementation of SME policy – the specially authorised body (central executive authority) and local governments.[5] Starting 30 March 2012, a new State Service for Regulatory Policy and Entrepreneurship (SSRPE) was given the mandate to implement government policies on entrepreneurship.[6] Until December 2010, the specially authorised body ensuring both implementation of state policy on entrepreneurship support was the State Committee of Ukraine for Regulatory Policy and Entrepreneurship (SCURPE). In addition, the new law sets the definition of SMEs in line with EU criteria, including a separate category for microfirms.

The legislative framework is developed around the National Programme for Small Entrepreneurship Development as well as the annual action plans, approved by the Cabinet of Ministers, which develop specific measures to support SMEs in Ukraine. Unfortunately, the one-year timeline of the action plan is too short to permit the government to pursue long-term goals and make long-term commitments. A multi-year strategic document would be preferable in order to set up a vision and clear objectives that could be achieved over four to five years. The previous strategic document, Concept of the State Policy for Small Business Development, expired in August 2004 and so far there have been no initiatives to develop a new one.

The implementation of the annual action plans is often incomplete due to insufficient and disproportionate allocation of funding. In 2008 and 2009 more than EUR 6 million[7] were committed from regional funds each year for the implementation of regional programmes, but only 53% and 28% respectively were actually allocated. In 2010, the amount actually allocated reached 75%, but the financial commitment stood at almost half compared to previous years.[8] Moreover, the instability and disproportionate allocation of funds prevent their efficient use. In 2010, 53.1% of regional funds were allocated in the last quarter of the year, which was reflected in the quality of the implemented actions.[9] The current practice of setting measures without taking into consideration the availability of state funds should be revised and measures should be reasonably matched to the financial resources available.

Ukraine has also embarked on several reforms that envisage the reduction of the informal economy, among other things. Recent reforms include the new Anti-Corruption Campaign and pension reform under review by the Ukrainian parliament, which aims to increase reporting on real salaries, encourage official employment and provide full-scale

allocations to the Pension Fund of Ukraine. The Customs Code of Ukraine is also currently under review with improvements aimed at reducing the number of permits required for customs control and customs clearance of goods. This should contribute to further formalisation of the economy. The new Tax Code, on the other hand, has proved to be controversial, negatively affecting SMEs and individual entrepreneurs in particular (see Box 18.1 for details). This, in turn, could lead small firms to opt for informality.

Box 18.1. **New Tax Code of Ukraine**

A new Tax Code was adopted in 2011 with the ambition to downsize the informal economy and fight corruption. However, several regulations have had an adverse affect, especially on individual entrepreneurs who are faced with greater administrative pressure as a result of additional reporting procedures:

- The subcontracting of individual entrepreneurs by legal entities will not refer to costs for the latter.
- The annual maximum turnover has been reduced to UAH 300 000 (previously UAH 500 000).
- Individual entrepreneurs are allowed to employ a maximum of four persons (formerly 10).
- The number of business activities allowed for individual entrepreneurs has been reduced (25 are no longer eligible).
- The consolidated taxes have increased. The individual entrepreneurs pay additionally around UAH 330 per month to their pension fund.

Source: Tax Code of Ukraine, in force since 1 January 2011.

Legislative simplification and regulatory impact analysis (RIA)

Ukraine has made some progress in the area of deregulation but more drastic measures are needed to meet EU standards. The Presidential Committee on Economic Reforms has approved Prosperous Society, Competitive Economy, a comprehensive package of economic reforms for the period 2010-14. The plan includes measures to review and simplify key areas of business-related legislation, and plans to introduce a number of legal acts aimed at simplifying administrative procedures. In response to the Law on Expedited Review of Regulations, the State Committee of Ukraine for Regulatory Policy and Entrepreneurship (SCURPE), the specially authorised body ensuring the implementation of state policy on entrepreneurship support, has also reviewed approximately 47 000 local regulations over a period of 90 days, and identified approximately 27 000 as inconsistent with state legislation. Looking ahead, a comprehensive plan for legislative simplification and regulatory guillotine should be developed and implemented by a competent public authority, addressing both primary and secondary business-related legislation.

The legal framework for RIA is outlined in the Law on Regulatory Policy in Economic Activity of 11 September 2003. It includes provisions to undertake cost-benefit analysis for draft regulations and periodic monitoring to determine the effectiveness of newly adopted legislation. Up to 2011, RIA was managed and conducted by SCURPE. Following the dissolution of SCURPE, these responsibilities have been transferred to the Ministry of Economy. Furthermore, the legal framework for RIA does not include any provisions for explicit consideration of the potential impact of new legislation on SMEs.

Public-private consultations (PPC)

In Ukraine, the most popular mechanisms for co-ordinated consultations are public hearings, but in practice their effectiveness is limited. Draft laws (including those that are SME-related) are usually discussed during parliamentary hearings organised by the profile committees of the Verkhovna Rada (Ukraine's parliament), where representatives of civil society and national executive authorities are invited to participate. Even though according to the law[10] the opinion of civil society should be taken into consideration when drafting legislative acts and regulations, their formal influence is weak.

Apart from public hearings, public-private consultations (PPC) in Ukraine are institutionalised within the framework of the Council of Entrepreneurs, whose activity has significantly decreased in the last year. The last meeting of the Council of Entrepreneurs took place on 12 May 2011. The council was founded in 2008 and consists of 68 representatives from various associations, unions and business representatives. Its structure is divided into thematic commissions that cover a range of business-related topics such as economic reforms, development of industrial sectors and humanitarian, social, scientific and innovative activities. The outcomes of the councils are not formalised and their activities do not have a significant impact on the policy-making process in the country. The council is also regionally represented by around 1 700 regional and local NGOs who contribute to public-private dialogue. In the regions the activity and influence of councils differs and often varies depending on the leader and the involvement of the members.

Establishing a conducive operational environment

The operational environment in Ukraine has deteriorated over the past two years. Administrative procedures are still cumbersome and costly and entrepreneurs are faced with significant opportunity costs before being able to start a business. In addition, e-government services, even though envisaged by legislation, are still far from being fully applicable.

Company registration

Company registration is a lengthy and cumbersome process in Ukraine, and efforts to introduce a more streamlined system have had a limited impact on the cost and efficiency of the registration process. The legal framework for company registration includes a number of measures to simplify administrative procedures for entrepreneurs. According to the Law on State Registration of Legal Entities, the State Registrar generates a single identification number and is responsible for completing all relevant notification procedures. In addition, amendments to the law recognising the electronic submission of registration documents were approved in October 2010.

During the pre-registration phase, entrepreneurs are typically required to notarise the company charter and registration documents, open a bank account for the initial capital, and pay the registration fee at a bank. Furthermore, although registration offices are widely available throughout Ukraine, one-stop-shops do not allow for the completion of all necessary notification and pre-incorporation control procedures. As a result, registration with the State Statistics Committee, the State Tax Authority and the District Tax Inspectorate must be undertaken separately. A total of 24 days and nine administrative procedures are required to complete the entire process. Further reforms should focus on

allowing all necessary registration procedures to be completed at one window of the one-stop-shops, and developing a functional website that offers online registration.

In Ukraine, the principle of tacit consent is introduced under the Law on Licensing in the Sphere of Economic Activity. Amendments to the Code on Administrative Violations were also passed on 17 February 2011. As a result entrepreneurs conducting business activities under the silence-is-consent principle are exempt from fines and punishment. These changes to the legislation were brought about by the Decree of the Cabinet of Ministers of Ukraine: Some questions on the application of the principle of tacit consent, dated 27 January 2010. However, the silence-is-consent principle is currently not included in the law on registration. Its introduction would send a clear signal to companies that registration procedures will be conducted within a reasonable timeframe, leading to a reduced administrative burden for SMEs.

Interaction with government services (e-government)

Electronic filing of tax returns is envisaged within the Tax Code of Ukraine, which was approved in December 2010. Online filing of social security contributions is also available through the Pension Fund of Ukraine. In practice, however, there are problems with the use of electronic signature, and the existing software and infrastructure are outdated and riddled with technical problems. At present there is no common legal framework for the development of online services such as pensions, procurement and cadastre. In order to encourage increased online communication between SMEs and the public administration, a comprehensive strategy is needed to ensure that state-of-the-art software and websites are in place for current e-government systems, and that new online mechanisms are developed to complement existing services.

In November 2009, the State Statistics Committee of Ukraine developed and approved an action plan to introduce online reporting of enterprise statistics. At present companies are able to file statistical reports online; however there is a need to increase the sophistication of current software and to encourage more widespread use by SMEs. The legal framework for electronic signature, including measures to allow for the establishment of certified accreditation bodies, was adopted by the government of Ukraine in 2003. At present firms are able to use e-signature when filing tax returns with the State Tax Authority; however there has been limited application of e-signature to other online services.

The government has developed a Single State Register to facilitate notification procedures during the company registration process. The system envisaged by the legislation aims to integrate the information generated during the registration process with the databases of various government bodies, including the State Statistics Committee, the State Tax Authority, the Pension Fund of Ukraine and the Social Security Fund. However, connections are not properly established between public institutions and, as a result, entrepreneurs are still required to register separately with the State Statistics Committee and the State Tax Authority. The development of an integrated system of internal communication between the databases of various offices of the public administration would greatly reduce the administrative burden for small businesses.

Bankruptcy procedures and second chance

Bankruptcy procedures are regulated by the Law on Restoring a Debtor's Solvency or Recognizing It Bankrupt of 14 May 1992 and revised on 31 June 1999. A new version of the

law is currently being developed and was approved on its second reading on 22 December 2011.[11] The main purpose of the revision is to make bankruptcy procedures more efficient and transparent and to better balance the interests of debtors and creditors.

The current system does not provide for quick and effective financial rehabilitation or liquidation of insolvent companies. On average, only 8.9% of creditors' claims are met, which is by far the lowest in the EaP region (28.2% across the region) while costs of proceedings are the highest (42% of the estate's value) according to the World Bank's *Doing Business 2012* report. In addition, court statistics show that about 90% of companies are usually wound up instead of being successfully restructured. This confirms critical claims made by a task group consisting of practicing experts[12] that the law is frequently being misused in fraudulent cases initiated by debtors to escape a creditor's claims, evade taxes or redistribute assets.

In terms of granting a second chance, there is no second chance campaign. However, there are no discriminatory provisions preventing entrepreneurs who have undergone non-fraudulent bankruptcy from re-starting and any natural person is free from debt after bankruptcy procedures have been completed. Re-registration as an entrepreneur or shareholder is possible without any restrictions including participation in public procurement tenders.

On the other hand, given the absence of a national bankruptcy filing system and the lack of formal discharge procedures, the law can easily be manipulated by dishonest re-starters as a tool providing unlimited opportunities to legally avoid payment of obligations. Moreover, expenditures accumulated in connection with bankruptcy proceedings in an arbitration court and the work of the liquidation commission and bankruptcy trustees take higher priority than a creditor's claims secured by mortgage. Also, tax debts take higher priority than claims of creditors that are not guaranteed by mortgage. Given also the high cost of proceedings, public authorities do not play a supporting role in debt settlement.

To achieve a more balanced approach, banks are lobbying for a change to Article 27 of the Law on State Registration of Legal and Natural Persons-Entrepreneurs, to ban those entrepreneurs who have undergone bankruptcy from re-registration for three years. Ideally, such an amendment would differentiate between honest entrepreneurs whose business has failed and those who are simply misusing regulations.

As of 21 November 2011, the Ministry of Justice of Ukraine has been designated as the focal point for all bankruptcy-related issues, including the creation (during 2012) and maintenance of a bankruptcy database (by decree of the Cabinet of Ministers of Ukraine of 16 November 2011). Similarly, a national system for filing bankruptcy is currently being developed. If properly enforced, these initiatives could lead to more equitable treatment of honest entrepreneurs looking for financial rehabilitation as well as strengthening creditors' rights.

Facilitating SME access to finance and developing the legal and business environment

Sources of finance such as bank lending, government support schemes, leasing and some equity finance are available in Ukraine. Nevertheless, Ukrainian SMEs, especially start-up enterprises, face important obstacles in accessing finance. The legal and regulatory framework in Ukraine has not been homogenously developed. The cadastre system has been developed whereas other areas such as the credit information system, collateral registration and creditors' rights are either insufficiently developed or still in the draft stage.

Sources of external finance for SMEs

Lending to SMEs is primarily provided by banks, among them Procredit bank which is mainly focused on SMEs. The banking sector is relatively large with assets proportional to GDP at 87%. Private sector credit to GDP amounted to close to 56% at the end of 2011. Prior to the financial crisis, several local banks actively expanded their lending to micro and small-sized enterprises through branches and outlets across the country. Additional mobile lending units have been serving rural SMEs and some banks provided specialised agricultural lending. However, general bank lending and lending to SMEs suffered significantly during the crisis as risk aversion increased. While lending growth is slowly recovering, commercial banks are generally reluctant to lend to SMEs.

Credit guarantee facilities are in place under the government's initiative and control. National programmes have been created by the Ukrainian government to introduce energy efficient technologies and to ensure product competitiveness in domestic and foreign markets. The State Export-Import Bank of Ukraine (Ukreximbank) implements national programmes for supporting SMEs. For the period from 2009 to 2011, the Ukrainian Fund for Entrepreneurship Support (UFES) established a UAH 12 million (USD 1.5 million) programme of public financial support on preferential terms to assist small businesses through Ukreximbank.

Public financial support for start-up businesses is available on a limited scale for the unemployed only. The Law on Mandatory State Social Unemployment Insurance provides a lump sum allowance if the unemployed start their own business.

Business angel activity is relatively minor in Ukraine. The Association of Private Investors of Ukraine, which was founded at the end of 2006, currently comprises 50 private and corporate investors with branches in five cities. However, the impact of its activity is currently limited. Plans to encourage business angels are in draft stage.

Aside from banks, credit unions and pawnshops are the primary providers of microfinance in Ukraine. There were 659 credit unions with 1.57 million members at the end of 2009. According to MIX, microlending was estimated at only 0.2% of GDP in 2011. Non-bank financial institutions are regulated by the State Commission for Regulation of Financial Services.

Leasing finance, although not fully developed as an alternative source of finance for SMEs, is among the highest in the region. In 2010 the Ukrainian leasing sector amounted to around 3% of GDP. Currently, 19 companies are active in the market, with the top three companies holding over 60% of market share. Most leasing activity takes place in the automotive sector. Although the Law on Financial Leasing has been in force since 1997, the lack of support schemes such as depreciation policy or tax incentives hinders growth in leasing of machinery and equipment.

The private equity market is gradually being established, in part through the entry of foreign private equity funds. However, both the number of market participants and the number of transactions remain low; there are less than five funds focused on Ukraine while a number of regional funds remain mostly passive. Committed capital and active capital were estimated at 0.5% of GDP and 0.4% of GDP respectively in 2010. Most of the committed capital is focused on growth investments with the presence of buyout and infrastructure. Legal initiatives aimed at supporting the availability of risk capital, such as the Draft National Programme on Development of Investment Activities for 2011-15, have been developed recently. Market institutions remain in the early stages of development, as

the corporate governance framework shows relatively low conformity with the OECD Principles of Corporate Governance.

Progress has been made to improve the quality of securities legislation since its adoption in 1996. However, its effectiveness is undermined by difficult court procedures and the lack of public procurement. In 2010, there were 183 companies listed on the Ukrainian Stock Exchange. The capitalisation of the stock market was 29% of GDP, but the stock is not readily convertible. A lack of open access to information on securities trading creates obstacles and limits their availability to the general public. The corporate securities market is affected by lobbying by oligarchic groups, a lack of transparency and poor corporate governance of enterprises.

Legal and regulatory environment

The cadastre system is in place but there is no unified automated system of land registration applicable to all land lots in Ukraine. Not all ownership titles of land are granted. The Law on State Land Cadastre, adopted in mid-2011 in order to speed property registration, requires that land registration be made prior to granting legal title to the owner. This law is the first step to a fully functioning cadastre and paves the way to lifting the ban on land privatisation.

The Law adopted in 2005 provides for the Bureau of Credit Histories to collect, maintain and use historical information relating to credit. Since then, three private credit bureaus have been established by financial institutions. The First Credit Bureau of Ukraine (FCBU) was founded in 2005 with the participation of the Association of Ukrainian Banks, 33 banks, two insurance companies, a leasing company and the CreditInfo Group. The FCBU manages credit histories of legal entities and private individuals and offers a wide range of specialised decision-making and risk management support systems. Another private credit bureau, the International Bureau of Credit History, was created on 6 April 2006. Finally, as in other countries in the region, Credit Info Ukraine is present in the country. It is a subsidiary of Creditinfo Group Hf. (CIG), an international holding company founded in 1997 in Iceland. The information maintained by the private credit bureaus is accessible exclusively by financial institutions. Information on debtors with obligations abroad is not included in this credit history. According to the World Bank's *Doing Business 2012* report, private credit bureaus cover 17% of adults.

A central state registry for movable charges is in place since 2004, although the information is only accessible subject to a fee.

Collateral requirements set by banks are currently high and are based on the borrower's level of risk. Generally only consumer loans are provided without collateral. Recently, the SME ProCredit Bank and the German development bank (KWF) are offering unsecured loans of up to UAH 80 000 with a 36-month maturity for financing SMEs' investments in energy efficiency.

The protection of creditors' rights remains one of the main challenges for Ukrainian banks. In mid-2011, a draft law introducing amendments to the Bankruptcy Law was adopted. This new amendment implies that secured creditors are now subject to the same claim filing requirements as other (unsecured) pre-bankruptcy creditors. Further efforts are required to enhance creditors' rights and ensure collateral enforcement through the court system.

Other factors that affect demand and supply of finance

In 2010, the InMind marketing research company, supported by USAID, carried out the National Survey of Financial Literacy. The survey, designed to assess the level of awareness and use of financial services and the understanding of consumer rights, revealed a poor level of financial literacy in Ukraine, including a lack of general knowledge as well as a lack of trust in the financial sector. A recommended national strategy for financial literacy has yet to be implemented.

Promoting a culture of entrepreneurship and skills development

This section summarises the human capital dimensions of the Small Business Act: entrepreneurial learning and skills for enterprises. It also addresses women's entrepreneurship.

Entrepreneurial learning

In the drive for a more entrepreneurial economy, the development of an eco-system for lifelong entrepreneurial learning (LL EL) in Ukraine requires that all parts of the education system, including those responsible for non-formal learning (self-employment promotion, start-up training) create a common development framework. This requires that each part of the learning system builds systematically on the entrepreneurial learning outcomes of earlier education. There is strong evidence and a commitment by education and training providers to address the promotion of entrepreneurship at various levels of the education system: there are some excellent examples in tertiary education, business lyceums and in non-formal learning. However, the assessment finds that connections between the various parts of the education and training system in terms of entrepreneurship promotion have yet to be established.

The range of practitioners, expertise and policy interest groups could be generated for a concerted dialogue involving all education levels on the one hand and government bodies responsible for education and economic policy, the private sector and civic interest groups on the other. Assuming that a framework approach to LL EL based on a multi-stakeholder partnership can be agreed, the education authorities should assume leadership and co-ordination of strategy building, activity planning and oversight of the monitoring process. The reporting line of the partnership to policy authorities or advisory arrangements, *e.g.* the Council for Entrepreneurship or line ministries would also need to be defined.

More attention should be given to integrating entrepreneurship into general education. Importantly, entrepreneurship should be addressed as a key competence (see Part II, Chapter 3) particularly in terms of curriculum reforms, teacher training and school governance, including links with business. To kick-start this process, the relevant authorities could consider borrowing from curriculum and assessment tools already successfully used within the EU and its pre-accession member countries. This could additionally demonstrate how the sharing of good practice, particularly amongst education and training providers (inside the formal schooling system as well as outside, for example where business support organisations play a role) can pay off in terms of time, cost and bringing innovation into the entrepreneurial learning arena. The experience of the Polish government-funded project School Entrepreneurial Academy (in which the 10 regions of Ukraine are involved) in the development of curricula to promote entrepreneurship key competence, teacher training and extra-curricula activities for the establishment of student entrepreneurial clusters in secondary education, could be scaled up.

Enterprise skills

The government of Ukraine has identified the anticipation of future skills demand as one of its priorities and is working on the development of tools and methodologies to analyse the overall demand. This will help in addressing the issue of more systemic developments in skills' intelligence in terms of skills gaps, skills weaknesses and future skills requirements and where the assessment pointed to the need for particular attention. Nonetheless, there are excellent examples of skills intelligence build-up which are project-driven (and where donor support is a defining feature) as opposed to being systemic developments, which the SBA indicator package recommends. Various regional, sectoral and project-based initiatives, which have developed and tested different tools and approaches for training needs analysis (TNA), would need to be consolidated with a view to formulating a nation-wide framework for TNA. A system approach to skills tracking in the small business environment would allow for improved policy decisions and better allocation of resources for training which would have immediate relevance to the economy, based on facts and figures on SME workforce skills.

While the training-provider market is well developed, there is clearly room for the private sector to assume some of the demand for training which is expected to increase as Ukraine's economy evolves. Sector-specific vocational and management skills will be important here, including more developed support for businesses keen to expand into new markets. This will be particularly important for trading with EU countries where market knowledge and training to ensure the necessary standards for products and services will be essential.

The assessment was not able to confidently determine the extent to which new start-ups have benefited from training support prior to business registration. To address this, the relevant authorities which hold responsibility for business registration could include a question in the business registration form which would quickly and systematically capture the extent to which new ventures have taken advantage of start-up training.

Finally, the assessment found good efforts in bringing forward quality assurance in the training market. A national qualifications framework was adopted in 2011 which could provide an important institutional pillar for further development of outcome-based quality assurance. While the current licensing and accreditation mechanisms are often seen as formal procedures for public training provision, many elements of the existing system could be tailored to support quality improvement of both public and private provision. Information on both accredited and non-accredited training providers is available on the websites of numerous regional and national websites of the authorities responsible for entrepreneurship support, employment services and business support institutions. Since 2007, Ukraine runs employer satisfaction surveys on the quality of university education programmes and publishes annual reports with rankings of best performing higher education institutions. This employer initiative has triggered a national dialogue to improve the quality and relevance of training provision across the education system.

Women's entrepreneurship

Promotion of women's entrepreneurship remains a defining feature of Ukrainian enterprise and economic policy. Earlier efforts to give greater prominence to women's contribution to the economy, and particularly to entrepreneurship training and support services, failed to ensure sufficient policy momentum to create any real impact. The crux

of the problem was first, that the promotion of women's entrepreneurship was designated as a gender issue in policy terms. This diluted the potential for the issue to feature within the country's competitiveness efforts. A second issue is that ministries with a policy interest in women's entrepreneurship (*e.g.* labour, economy) work independently; co-ordination of policy effort and resources would bring efficiencies to maximise the country's effort to improve women's entrepreneurship. Finally, although a number of networks have interest and experience in promoting women's entrepreneurship, none plays a sufficiently significant policy advocacy role to give greater prominence to critical areas such as training and access to finance.

A next review and updating of enterprise policy in Ukraine should include a chapter specifically addressing women's entrepreneurship and underlining the role and potential of women in start-ups and developing businesses. The policy chapter should be followed up with resources that ensure that start-ups and growing businesses led by women are given fair access to support services (*e.g.* training, mentoring, advisory) and finance. Finally, to reinforce a Ukrainian policy drive for women's entrepreneurship, existing networks should be audited to determine if and to what extent they could assume a professional policy advocacy role.

Enhancing SME competitiveness

There is limited public support for SMEs in Ukraine. Most of the tools aiming to enhance SME competitiveness are envisaged in basic strategic documents but many of them may not be fully implemented due to a lack of funding.

Business information and services

The provision of services by the public sector in Ukraine is conducted within the framework of the Annual Action Plan for implementation of the National Programme to Promote Small Business in Ukraine (2000). This plan envisages the development of an infrastructure for small business. The action plan usually includes advisory services and consultations in the areas of business planning, accountancy, taxation, lending, management, marketing, as well as development of an SME support infrastructure and rental of space at preferential rates. At the local level, the tax service has established advisory offices, providing free consultancy for established entrepreneurs, legal entities and start-ups.

Despite a number of government initiatives to provide business services, the range of services for SMEs is very limited and most are not implemented due to a lack of funding. Overall, in 2009-10, only 15.8% out of the total financing of the regional programmes was used for informational support, training, organisation of seminars, conferences and participation of entrepreneurs in trade fairs, while 3.6% was allocated to the creation and maintenance of the existing SME support infrastructure; (80% was allocated for financial and credit support of SMEs). In addition, in order to implement the regional programmes for SME support in Ukraine, the organisations must register as a unit of SME support infrastructure according to the 2009 Resolution of the Cabinet of Ministers of Ukraine. As of 1 January 2011, the SME support infrastructure included 438 business centres, 69 business incubators and innovative business incubators, 43 technoparks, 245 entrepreneurship support funds, as well as financial institutions, innovative investment funds and companies, consulting centres, entrepreneurs' associations and other organisations.

Apart from public support, most business service providers on the market are private enterprises. Their services are limited to those demanded by large companies, such as accounting and legal advice. The quality of business services and trainers' qualifications in Ukraine is not regulated or certified, unless the company itself chooses to follow international or internally approved standards.

Ukraine has no unified online portal on business information for SMEs. Information on business services providers is partially available on the still operational website of SCURPE and on the website of the Fund for Entrepreneurs Support. However, neither of these websites consolidates all the information or links into a single portal that could be useful for an SME or entrepreneur. The information centres currently operating are mostly private and are not accredited by the related national authority. They are therefore not easily accessible to SMEs.

Even though the national programme does not envisage services for start-ups, the State Employment Office provides specialised business development services for start-ups offering free courses which cover the main aspects of starting up and doing business. In addition to start-up training, the unemployed person may receive a one-time lump-sum payment of unemployment allowance for entrepreneurial activity.[13] However, the use of these funds is not monitored and it is not clear to what extent they are indeed used for entrepreneurial activities.

According to data presented by local authorities, on 1 January 2011 the SME support infrastructure network included only 69 business incubators, with the highest density in Kyiv (13 per 10 000 inhabitants). In Ukraine there is no legislative framework for the regulation of incubation activity, and for the time being services provided by business incubators are not certified in Ukraine. Aspects of business incubator development should be considered as an integral part of SME development policy and its legal framework.

Public procurement

Ukraine has a comprehensive framework regulating public procurement which was adopted on 1 June 2010. It is open to foreign and domestic economic operators on an equal basis. Notwithstanding the *de jure* possibility of cutting tenders into lots, the questionnaire response does not provide evidence for its implementation.

It is not clear whether enterprises are allowed to participate in joint bidding in public procurement, for example to form consortia that allow them to fulfil technical and financial requirements.

No information was received concerning late payments.

A dedicated web portal (*www.tender.me.gov.ua*) is run by the Ministry of Economy and is the authorised agency co-ordinating the procurement of goods and services for public funds. It places advertisements about upcoming public procurement. Information is free but prior registration is required. It is not clear to what extent e-procurement practices are popular and widely used.

Innovation policy

According to Presidential Decree 437/2011, the State Committee for Science, Innovation and Information is responsible for the implementation of innovation policy and technology transfer in Ukraine. The activities of the committee are co-ordinated by the Cabinet of Ministers of Ukraine and the Minister for Education, Youth and Sports. In

addition, the National Academy of Sciences and the State Agency for Investment and Management of National Projects are also involved in the promotion and implementation of innovative activities in various areas and capacities.

A general strategy for innovation policy was approved on 8 September 2011 within the Law on the Priority Directions of Innovation Activity in Ukraine. The law defines priorities for the development of new technologies and innovations over the period 2011-21. However, innovation policy is currently fragmented into over 70 legal documents and acts, and there is a clear need for greater co-ordination and consolidation of strategic approaches. Further development of innovation policy can be achieved by approval of a more detailed strategy and action plan, with clear information on implementation plans and timelines for completion.

The government has established a number of technology parks and research centres in Ukraine, under the state programme Establishment of Innovation Infrastructure in Ukraine for 2009-13. The programme is funded by contributions from the state, local governments, the private sector and international organisations. Although the programme envisages an integrated system of co-operation between all key stakeholders, in practice small businesses and higher educational institutions do not engage in collaborative efforts to innovate.

A limited number of donor-funded innovation support schemes operate in Ukraine. For instance, the EU-funded project Support to Knowledge-based and Innovative Enterprises and Technology Transfer to Business in Ukraine stimulates technology transfer by developing links between research centres and industry. Although financial support for innovation is envisaged within the legislation, in practice SMEs have significant difficulty in financing innovative projects. SMEs may obtain some limited funding through the Ukrainian Fund for Business Support, the Ukrainian State Farmers Support Fund and the Ukrainian State Innovation Fund. However, there is a need to develop a more comprehensive portfolio of government-funded support schemes for innovative SMEs.

Green economy

Various governmental activities have been developed to include green economy concepts in official policy documents and legislation, *i.e.* national action plans for the implementation of cleaner production in Ukraine for the years 2012-14 and of environmental protection in 2012-15.

Information on environmental legislation and specific programmes is mainly provided by the government. A national Action Plan on Environmental Protection is in force which has created a national information system on environmental protection and has promoted the development of information centres. A network to access environmental information is envisaged for 2015.

Finally, the government provides information on environmental management standards (EMS), but this information is not particularly aimed at SMEs. There is no information on how many companies have made use of EMSs.

Export promotion

An action plan to support export activities of small and medium-sized business entities for 2009-11 was approved by the government of Ukraine in 2009. While national and local authorities were nominated to implement the action plan, no funds were

allocated and it was not implemented. The action plan stipulated a number of measures required to encourage small firms to export, *e.g.* improving the legal and regulatory framework of state promotion of export activities, financial and credit support for export activities, improving taxation policy and information and advisory support for exporters.

No other significant actions have been undertaken to introduce state financial instruments to support SMEs' export activities. The Order of the CMU On Approval of the Action Plan to Introduce Principles of the Small Business Act for Europe, regarding export promotion, envisages improvements to the website and the Complex System of Information and Advisory Support and Export Development aims to facilitate access to information on goods of Ukrainian origin for national and foreign SMEs.

Up until 2009 large nationwide forums such as Government and Business are Partners were held regularly (1-2 times a year from 2005). Until its dissolution in December 2011 SCURPE was the main facilitator of national level SME promotion events, such as the celebration of Entrepreneurs Day. Participants in these events were representatives of business, associations of entrepreneurs, scientists, the president of Ukraine, the Prime Minister and other top-level officials. Several of these forums potentially could have had an impact on encouraging improvements within the SME sector but this initiative turned out to be purely promotional. At the moment, due to institutional restructuring, it is unclear whether more such events will be organised in the future.

Single Market opportunities

Technical barriers to trade and sanitary and phytosanitary standards (SPS) are important chapters of the Deep and Comprehensive Free Trade Agreement (DCFTA) as part of a future Association Agreement between the EU and Ukraine. Negotiations on the DCFTA were concluded in 2011, demonstrating the considerable progress already made on regulatory convergence in these fields.

New laws on market surveillance and control of non-food products and of non-food product safety entered into force in July 2011. In addition, the pre-market control of manufacturers was abolished. The law on liability for damage rendered by defective products came into force in 2011.

Amendments to the metrology law were submitted to parliament; they preserve the existing non-transparent system burdened with conflict of interest issues. Technical regulations based on EU directives need revision to be fully compliant.

Ukraine made progress in gradually converging with EU SPS standards. An institutional reform plan was prepared to obtain EU support under the Comprehensive Institution Building programme. The Veterinary and Phytosanitary Service was consolidated and staff were trained with EU support.

SMEs are informed on the website of the Ministry of Economic Development and Trade of export conditions and opportunities for Ukrainian enterprises planning to engage in the EU.

The way forward

Based on the SBA assessment, Ukraine could consider the following steps to ensure continuing progress in the area of SME development:

- Although the National Action Plan for Implementing Economic Reforms (approved on 27 April 2011) states several activities aimed at improving the business climate, it is

unlikely that progress will be achieved without a clear commitment to the SME sector. Ukraine would benefit from the **elaboration of a viable long-term SME development strategy** including the creation of a more enabling legal environment to encourage small business development. Most importantly, the necessary resources have to be allocated and a specialised body assigned to ensure the implementation of the strategy. In order to ensure its effectiveness, a monitoring and evaluation scheme needs to be developed based on clearly defined objectives and measurable indicators. The SME strategy should also cover aspects of human capital development, women's entrepreneurship and elements of the green economy.

- The mechanisms for **public-private consultations** need to be strengthened and private sector influence on regulatory decisions needs to be increased. Developing tools to ensure the broader participation of the private sector, and in particular SMEs, in creating a relevant legal environment should be a priority for the efficient deliberation of small business issues.[14] The influence of the Council of Entrepreneurs under the Cabinet of Ministers would need to be strengthened and its activity regulated to ensure that consultations take place on a regular basis, discussion topics are submitted early enough for the private sector to provide comments, and alternative proposals, comments and recommendations are taken into consideration.
- **A concerted approach is needed to ensure that each part of the lifelong learning system contributes systematically to entrepreneurial learning outcomes**, supported by a multi-stakeholder partnership and benefitting from government leadership and continuous support. Key competence in entrepreneurship requires attention within the overall context of education and modernisation of training, particularly through reforms in curricula, new approaches to teacher training and by exploring new forms of co-operation between entrepreneurial schools.
- More consideration must be given to the provision of **public support to SMEs in the form of business services and informational assistance**, particularly in the areas of services that are not provided by the market. More specifically, specialised services and training for start-ups could be organised within the framework of the annual action plans. Budget allocations would need to be increased to ensure that public support services can be delivered to SMEs. Given the recent changes in the executive bodies of the government and a wide range of reforms in the area of business environment, creation of an online portal specifically designed for SMEs could help SMEs get information and shed some light on recent changes and upcoming opportunities.
- **Further improvements in corporate governance and the business environment would facilitate the development of equity capital.** Improvements in the legal framework for leasing and product development is important to increase leasing activity. Better access to information from the private credit bureau and collateral registry could significantly improve access to finance for SMEs. Ensuring creditors' rights to allow secured creditors to seize their collateral after re-organisation and to be paid out first from the proceeds of liquidation of a bankrupt firm is important to encourage banks to increase lending in general and to SMEs in particular.
- **The innovation policy framework in Ukraine needs to be consolidated.** To address this, a more detailed strategy and action plan would be required, with clear information on implementation plans and timelines for completion. To be implemented, innovation support services to SMEs would require additional funding. Ideally, such funding

mechanisms would encourage bottom-up initiatives rather than distributing R&D funds top-down to a limited number of research institutions. This would ensure that scientific research outcomes lead to the practical applications needed by the market.

Notes

1. EBRD macroeconomic indicators, registered unemployment only.
2. Exports by economic sectors: *http://ukrstat.org/operativ/operativ2011/zd/tsztt/tsztt_r/tsztt0811_r.htm*.
3. These data are based on the information from the State Tax Service of Ukraine and include farms and individual entrepreneurs.
4. No data are available on the overall share of SMEs across sectors.
5. This includes also the Autonomous Republic of Crimea.
6. Other responsibilities of the State Service for Regulatory Policy and Entrepreneurship are the supervision and control of economic activities, implementation of regulatory policy and issuing of permits and licences, based on Decree of President of Ukraine from 30 March 2012 N237/2012 on Approval of Provisions for the State Service for Regulatory Policy and Entrepreneurship.
7. UAH 75 and 72 million (EUR 6.8 and 6.5 million) respectively.
8. *www.dkrp.gov.ua/control/uk/publish/category?cat_id=98818*.
9. *www.dkrp.gov.ua/control/uk/publish/category?cat_id=98818*.
10. Resolution of the CMU of 3 November 2010, No. 996, "On Ensuring Citizen Participation in State Policy Formation and Implementation".
11. *http://pravoznavstvo.at.ua/news/nova_redakcija_zakonu_pro_vidnovlennja_platospromozhnosti_borzhnika_ta_viznannja_jogo_bankrutom/2011-12-22-147*.
12. The Task Group includes representatives of the Union of Ukrainian Crisis Managers, the National Trade Union of Court-Appointed Trustees, the Commercial Law Center, and the Foundation for Effective Governance, a number of law firms and members of parliament. *www.feg.org.ua/docs/NewsletterIssue12_en.pdf*.
13. Another reason for these payments might be to reduce official unemployment figures, as the person who receives the lump sum is automatically considered to be an entrepreneur and removed from the unemployment register.
14. A project with the support of Norway in Kyiv: Support in involving entrepreneurs in the decision-making process of the government authorities, was allocated UAH 86 300 and UAH 3 500 by the Ukrainian Fund for Entrepreneurship Support.

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ANNEX A

Small Business Act assessment framework

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
I)	***Create an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded***						
	Policy framework for entrepreneurial learning (EL)						
1.1.1.	Policy partnership	No structured co-operation between public, private and non-governmental sectors on EL.	An ongoing national dialogue with view to structure co-operation between public, private and non-governmental sectors on EL.	A national EL partnership has been established between public, private and non-governmental sectors to promote entrepreneurial learning.	State funds ensure sustainable contribution of EL partnership to national developments (*e.g.* administrative support, work plan, capacity development).	An EL partnership advises on a range of national strategies (education, employment, SME, R&D) and action plans.	3
1.1.2.	Good practice exchange[1]	There is no systematic exchange of good practice between lifelong EL providers.	A national network of life- long EL providers meets on a regular basis to exchange good practice.	Examples of adapted EL good practice (domestic and/or international) are being piloted in the country.	Results of domestic good practice are being disseminated nationally (at least one annual event).	Within the reporting period, at least one domestic good practice has been transferred to another education and training environment in a neighbouring country, European Union or beyond.	1
1.1.3.	Non-formal learning	Examples of actions to promote non-formal EL (privately and/or publicly supported).	A working group monitors non-formal EL as part of national EL strategy and advises on improvements. Evidence of at least one quarterly, high-level press coverage (national newspaper or TV) of EL policy or delivery.	Examples of agreements established between public authorities, enterprise, community groups or philanthropic organisation to develop entrepreneurial spirit and skills across society with particular reference to children and young people.	At least one annual, high-profile event at national level to promote awareness and information on broader EL (*formal and non-formal*) to show-case successful projects. High-profile event includes national recognition or awards for EL practice.	Transfer of know-how: principles or *practice* from at least 2 of the *non-formal* show-case projects from the previous year's high profile event are integrated into other EL environments national or internationally.	1
	Upper secondary education (ISCED 3)						
1.1.4.	ISCED 3 Entrepreneurial learning (EL)[2]	EL in upper secondary education (entrepreneurship key competence and business skills) is confined to *ad hoc* projects which are not part of mainstream education curricula.	EL in upper secondary education (entrepreneurship key competence and business skills) is confined to school-based individual initiatives which are known to the education authorities.	EL (entrepreneurship key competence and business skills) is an integral feature of the national curriculum which specifies entrepreneurship key competence and elective EL subjects.	EL (as a key competence and business skills) is included in teaching plans of at least 50% of upper secondary schools. Evidence for this level will be drawn from schools' Annual Reports (Monitoring and evaluation sub-indicator).	EL (as a key competence and business skills) is included in teaching plans in at least 70% of upper secondary schools. Evidence for this level will be drawn from schools' Annual Reports (Monitoring and evaluation sub-indicator).	2

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
	Women's entrepreneurship						
1.1.5.	Policy support framework for promotion of women's entrepreneurship	Fiscal, economic, employment, social, and education and training polices are not gender-sensitive. No structured dialogue between government and stakeholders,[3] nor institutional support structures, in place to promote policies[4] and measures for women's entrepreneurship. Data framework for an integrated policy environment (fiscal, economic, employment, social, education and training), essential for promoting women's entrepreneurship[5] is not in place.	Government and key stakeholders have engaged in a policy reflection process with the objective of setting up a co-ordinated and mutually-reinforcing gender-sensitive policy environment to improve women's entrepreneurship. Policy reflection process includes analysis and options to maximise the interface and synergies between national fiscal, economic, employment, social and education and training polices. Draft regulatory fiscal, economic, employment, social and education and training polices are being reviewed for gender sensitivity. Policy improvement recommendations have been defined for ensuring gender sensitivity within fiscal, economic, employment, social and education and training polices for more developed women's entrepreneurship.	A women's entrepreneurship policy framework incorporating the gender-sensitive policy improvements (Level 2) has been approved by government and key stakeholders. A medium-term action plan with clearly defined measures for each of the policy areas (fiscal, economic, employment, social and education and training) to include a women's entrepreneurship consultation forum and information and networking measures has been approved by government and key stakeholders. Government offices responsible for polices (fiscal, economic, employment, social and education and training) supporting women's entrepreneurship have *each* committed annual budget to follow through on planned actions for policy implementation. A dedicated institutional support structure oversees: *a)* the implementation of the gender-sensitive fiscal, economic, employment, social and education and training policies; *b)* collects data for the respective policy areas; and *c)* reports annually to all stakeholders on policy progress with an action plan.	In the reporting period, each of the government offices responsible for their respective policy areas (fiscal, economic, employment, social and education and training) demonstrates progress in the implementation of measures as defined in the action plan. Government funding is available for implementation of the measures for each of the policy areas (fiscal, economic, employment, social and education and training).	A national policy and supprt framework for women's entrepreneurship is fully established with a rolling work programme with financial support from each of the government offices responsible for each of their respective policy areas (fiscal, economic, employment, social and education and training). The framework includes evidence-based monitoring and evaluation arrangements with clear reporting lines on each policy area (fiscal, economic, employment, social and education and training) by the respective government offices. On an annual basis, government offices with responsibility for each of the policy areas (fiscal, economic, employment, social and education and training) along with key stakeholders: *a)* review progress and constraints on each of the respective policy areas using data and other evidence available; *b)* determine policy improvement points; and *c)* agree on measures for implementation in the subsequent 12 months.	3

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
II)	***Ensure that honest entrepreneurs who have faced bankruptcy quickly get a second chance***						
2.1.	**Bankruptcy procedures**						2
2.1.1.	Laws and procedures on distressed companies, receivership and bankruptcy	No specific laws and/or other procedures on distressed companies, receivership and bankruptcy.	Distressed company, receivership and bankruptcy laws and/or procedures in drafting stage.	Distressed company, receivership and bankruptcy laws and/or procedures formally in-place. Legislation not systematic and at an early stage of implementation.	Evidence of implementation of distressed company, receivership and bankruptcy laws and/or procedures in line with international standards and fully integrated in and consistent with commercial law and practice. Backlog of old cases has been reduced. Bankruptcy procedures also apply to state-owned enterprises.	Distressed company, receivership and bankruptcy laws and/or procedures effectively and systematically applied in a transparent way. Bankruptcy procedures also apply to state-owned enterprises. There is ample evidence for this.	1
2.1.2.	Bankruptcy Time (DB indicator)	Bankruptcy time is more than 4 years.	Bankruptcy time is more than 3 years but less than 4 years.	Bankruptcy time is more than 2 years but less than 3 years.	Bankruptcy time is more than 1 year but less than 2 years.	Bankruptcy completed within a year (1.7 years is the average of the OECD countries).	1
2.1.3.	Cost (% of the estate) (DB indicator)	Costs are more than 25% of the estate.	Costs are more than 20% but less than 25% the estate.	Costs are more than 15% but less than 20% of the estate.	Costs are more than 8% but less than 15% of the estate.	Costs are less than 8% (9.1% is the average of the OECD countries).	1
2.1.4.	Recovery rate (cents on the dollar) (DB indicator)	Recovery rate is less than 25% of the estate.	Recovery rate is less than 40% but more than 25% of the estate.	Recovery rate is less than 55% but more than 40% of the estate.	Recovery rate is less than 70% but more than 55% of the estate.	More than 70% (69.1% is the average of the OECD countries).	1
2.2.	**Second chance** *http://ec.europa.eu/enterprise/policies/sme/business-environment/failure-new-beginning/index_en.htm*						1
2.2.1.	Promoting positive attitude towards giving entrepreneurs a fresh start	The public administration has no information campaign on second chance.	Some measures exist but at local, regional, sectoral level with no co-ordination. No overall national strategy exists.	A package of measures to promote second chance is under preparation.	Information campaigns are in place on second chance and some measures to help entrepreneurs start afresh (information on procedures, training, etc.).	Information campaigns are in place on second chance and well developed measures to help entrepreneurs start afresh (information on procedures, training, etc.).	1
2.2.2.	Discharge from bankruptcy	Discharge from bankruptcy is not determined.	The discharge procedures are under consideration.	Discharge procedures exist and a clear indication of maximum time for full discharge is present in the legislation.	Full discharge from bankruptcy is possible within a maximum of 3 years after final court decision.	Full discharge from bankruptcy is possible within a maximum of 3 years after final court decision. Removal from bankruptcy register is automatic and removal from national credit rating black list is automatic within maximum 1 year after full discharge.	1
2.2.3.	The role of public authorities (taxation) in supporting a quicker debt settlement	Tax debts take first priority over any other debt in a bankruptcy.	All tax debts take first priority but payment by instalments is available.	Some tax concepts (fees, arrears, interests, licenses) take lowest priority.	Most tax concepts including corporate taxation take lowest priority.	Only social security debts take maximum priority. The rest take lowest priority.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
III)	***Design rules according to the "think small first" principle***						
3.1.	**Institutional framework**						3
3.1.1.	SME Definition	No definition for SMEs exists.	A law to define SMEs is under preparation.	Different definitions for SMEs are used by different public authorities.	Definition for SMEs is consistent in all legislation and takes into account adequate variables.	Definition for SMEs applies similar criteria as the definition for EU members (employment size, assets size, and turnover) approximated to country specificities.	2
3.1.2.	Availability of statistical data on SMEs	No statistical data on SMEs available.	Only basic information available (number, employment, value added), based on business registries.	A wider range of indicators is available (turnover, expenditures, profits, exports share) based only on business registries.	A wide range of indicators is available on request both from business registries and surveys (*i.e.* informal sector taken into account).	A wide range of data is available online both from registries and surveys.	1
3.1.3.	Inter-governmental co-ordination in policy elaboration	No institution is responsible for SME policy elaboration.	Several institutions are responsible for SME policy elaboration and they have overlapping portfolios and limited co-ordination.	Approval for establishment of a single institution in charge of leading and co-ordinating SME policy elaboration.	Single institution in charge of SME policy elaboration in place and fully operational. System of consultation with the implementing agency (ies) in place.	Level 4 + effective mechanism of policy co-ordination involving key ministries, agencies and local administrations, *e.g,* by nominating an SME Envoy, when relevant.	3
3.1.4.	SME development strategy[6]	No SME development strategy exists.	SME development strategy is under elaboration. Review of expired SME strategy under way.	Multi-year SME development strategy for current period is approved by the government and at initial stage of implementation. Budget established but entirety of funds not yet received.	Solid evidence of implementation of the SME development strategy with indication of key targets achieved and assignments completed. Entirety of funds received and in process of being disbursed.	A pro-active SME development strategy accompanied by significant evidence that all components of the strategy have been implemented, as demonstrated by time-bound targets achieved and number of assignments completed. SME strategy has a demonstrated impact and has strengthened the SME sector.	3
3.1.5.	SME policy implementation agency or equivalent	No SME policy implementation agency with an executive role (or equivalent) exists.	Government considering the establishment of an SME policy implementation agency (or equivalent).	SME implementation agency (or equivalent) established. Staff, structure and budget in place. Range of output to be covered by agency being drafted.	SME implementation entity fully operational and covers a range of activities with measurable outcomes. Staff is complete and the required expertise (economic and legal) is in place. Solid implementation record of SME strategy based on achievements of time-bound targets as detailed in action plan.	SME implementation entity is the main body for implementation of the SME strategy, operating with full political support. The entity has a clear reporting system in place and a recognised advocacy and policy advice role. The entity is well-funded, wide-reaching, and its activities have proven to be effective in supporting SME development with measurable outcomes.	3
3.1.6.	Measures to tackle the informal economy	No measures in place to systematically tackle the informal economy.	Plan in preparation to tackle the informal economy.	Plan to tackle the informal economy has been adopted after inter-ministerial and stakeholder consultation. Action plan defined.	There is evidence that elements of this plan have been implemented.	Implementation well advanced and monitoring systems in place to measure the impact of the plan.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
3.2.	**Legislative simplification and regulatory impact analysis**						
3.2.1.	Review and simplification of current legislation	There are no plans to review and simplify current primary or secondary business related legislation with an impact on SMEs.	There has been *ad hoc* activity to carry out the simplification of regulations, but no concrete plan exists yet.	A concrete plan to review and simplify business related legislation with an impact on SMEs has been approved and institutions in charge have been identified.	Implementation of the plan to review and simplify business related legislation with an impact on SMEs is ongoing.	Legislative review well-advanced and extended to secondary legislation.	3
3.2.2.	Legislative guillotine	There are no plans to reduce legislation related to SMEs.	There has been *ad hoc* activity to carry out elimination of redundant and obsolete legislation and regulations, but no concrete plan exists yet.	A concrete plan to carry out systematic elimination of redundant business related legislation and regulations with an impact on SMEs has been approved and institutions in charge have been identified.	Regulatory guillotine process has started and has successfully eliminated the redundant regulations in primary business related legislations.	Regulatory guillotine process well advanced and extended to secondary business related legislation with an impact on SMEs.	3
3.2.3.	Use of regulatory impact analysis (RIA)	No systematic regulatory impact analysis exists.	Proposal for a law on RIA exists. A simplified, pilot RIA programme is being used in certain areas of regulation.	Approval of law on RIA. The RIA applied is limited in scope and is restricted to simplistic techniques (*e.g.* inter-ministerial meetings, consultation with interested parties). There is no preceding analysis on what technique is most applicable and the RIA process is poorly structured.	Implementation of RIA in some areas. There is some evidence that the outcomes of the RIA have been used to change or cancel legislation.	RIA is systematically implemented. There is ample evidence that the outcomes of RIA have been used to change or cancel legislation. RIA is also applied *ex post* to measure the impact of legislation during the implementation stage.	3
3.2.4.	The SME test[7]	The SME aspects are not considered under RIA.	There is a pilot project on the SME test.	There is a formal requirement to examine SME aspects in business related legislation.	The SME test is implemented on limited number of pieces legislation.	The SME test is systematically applied and there is ample evidence that the outcomes of RIA have been used to change or cancel legislation.	1
3.3.	**Public-Private Consultations (PPCs)**						
3.3.1.	Frequency and transparency of public/private consultation (PPCs)	Consultation between the public and private spheres occur sporadically/*ad hoc*.	Proposals have been made to establish a structure/framework for public/private consultation.	A regulation(s) has/have been adopted which stipulate(s) regular consultation between public and private spheres including with SME associations.	Consultations involving key actors from public and private sector take place on a quarterly basis. The private sector is responsible for designing part of the agenda independently and can call for an exceptional meeting several times per year when deemed necessary. A detailed record of the meetings is kept.	Level 4 + the consultations take place on a monthly basis or more. The documents are made available by the government with at least 8 weeks prior to making any legislative and adm. proposal to the parliament that has an impact on businesses. The outcome of meetings and decisions is announced on government websites. Communiqués and meeting minutes are widely accessible (*e.g.* published on a website).	1
3.3.2.	Formal influence of PPCs	PPCs take the form of unstructured debates between the public and private sector.	Level 1 + the private sector has the opportunity to give formal recommendations on the issues discussed.	Level 2 + the private sector has the opportunity to formally comment on draft SME legislation in those meetings.	Level 3 + there is ample evidence that the comments on draft legislation are integrated + the private sector can suggest own initiative draft laws or measures on SME policy.	Level 4 + there is ample evidence that suggestions on own initiative draft laws or measures from the private sector have been realised.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
3.3.3.	Representativity of PPCs	Few, randomly selected companies are invited to the PPCs. The access to the PPCs is thus restricted and there is no system of disseminating the information about upcoming PPCs to the private sector.	Invitations to the PPCs are targeted, however mainly to big and influential companies and selected associations. Some attempts are made to inform the private sector about upcoming PPCs (*e.g.* announcements on government website) but access is still restricted.	Invitations to the PPCs are targeted to selected companies and associations but information about upcoming PPCs is publicly available and registration is open to interested participants.	Invitations to the PPCs are distributed to a wide range of companies and independent private sector associations which have been mandated by the private sector to represent the interests of the business community across different sectors.	The PPCs consist of a forum that is broadly representative of the private sector and includes the SME community (different sectors, different company sizes, chambers of commerce, etc.). Comprehensive and widely accessible structures are in place to inform the private sector about upcoming PPCs.	1
IV)	***Make public administration responsive to SMEs***						
4.1.	**Company registration**						
	Issuing of company registration certificate						2
4.1.1.	Number of days for obtaining company registration certificate	Registration in more than 30 days.	Registration takes more than 15 days, but less than 30 days.	Registration takes more than 5 days, less than 15 days.	Registration takes less than 5 days, but more than 1 day.	Registration in 1 day.	1
4.1.2.	Number of administrative steps for obtaining a company registration certificate	Registration requires more than 10 administrative steps.	Registration requires 8-9 administrative steps.	Registration requires 5-7 administrative steps.	Registration requires 2-4 administrative steps.	Registration requires only 1 step.	1
4.1.3.	Official cost of obtaining the company registration certificate	More than EUR 250.	Less than EUR 250, more than EUR 150.	Less than EUR 150, more than EUR 50.	Less than EUR 50, more than EUR 10.	Less than EUR 10.	2
	Company identification numbers						1
4.1.4.	Administrative identification numbers in dealing with the public administration	5 registrations and identification numbers in dealing with different administrative authorities (statistical office, customs, labour office, tax office, etc.).	4 identification numbers in dealing with different administrative authorities. Some registrations merged.	3 identification numbers in dealing with different administrative authorities. Half of registrations merged.	2 identification numbers in dealing with different administrative authorities. Most of registrations merged.	Single identification number in dealing with all standard functions of public administration – single registration process.	1
	Completion of the overall registration process and entry in operations						1
4.1.5.	Number of days for completing the overall registration process, including compulsory licences for standard business activities (WB, *Cost of Doing Business Index*)	Registration takes more than 30 days.	Registration takes more than 15 days, but less than 30 days.	Registration takes more than 5 days, less than 15 days.	Registration takes less than 5 days, but more than 1 day.	Registration takes 1 day.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
4.1.6.	Costs connected with registration (% of GNI per capita) – (WB, *Cost of Doing Business Index*)	Costs are more than 10% of GNI per capita.	Costs are between 5% and 10% of GNI per capita.	Costs are between 2.5% and 5% of GNI per capita.	Costs are below 2.5% of GNI per capita.	Costs are minimal (close to 0 of GNI per capita).	2
4.1.7.	Minimum capital requirements (% of GNI per capita) – (WB, *Cost of Doing Business Index*)	More than 40% of GNI per capita.	Between 20% and 40% of GNI per capita.	Between 10% and 20% of GNI per capita.	Less than 10% of GNI per capita.	No minimum capital requirements for general partnerships with personal liability.	2
	Advanced company registration process						1
4.1.8.	Progression to one-stop-shop (OSS)	There are no plans to introduce one-stop-shop (OSS) for company registrations.	Legislation is in drafting stage to establish OSS for company registration and there are plans to adopt legislation.	The necessary legislation and budgetary provisions to establish a OSS for company registration has been approved.	OSS for business registration operates on the basis of multiple window in one location or with a limited geographic scope.	OSS for registration is operational with a proven track record and extensive geographic scope. OSS completes all necessary registration and notification procedures in one window (one step).	3
4.1.9.	Online registration	The government has not taken any steps towards the introduction of online registration.	Evaluation of existing administrative procedures and detailed proposals for the introduction of online registration. Budget provisions and pilot project.	Law on online registration, action plan and budget provisions approved. Designation of competent authority.	Level 3 + solid evidence of implementation of online registration; system available only in some regions.	Level 4 + complete implementation of online registration; system fully integrated with other services of e-government and available throughout the country. Online registration applies to all phases of the company registration process.	2
4.1.10.	Silence-is-consent principle	The principle is not used in standard administrative practice.	Evaluation of current procedures and detailed proposals on the introduction of the silence-is-consent principle.	Approval of law on silence-is-consent.	Solid evidence of implementation of the silence-is-consent principle in key areas/sectors of the administration.	Full implementation and widespread use of the principle in many areas/ sectors of the administration. Regular reviews (involving business sector) to identify new areas where the principle could be adopted.	1
4.2.	**Interaction with government services (e-government)**						
	E-government services						2
4.2.1.	Tax returns	Tax returns can not be filed online.	Government is considering proposals to allow for online filing of tax returns. Pilot project.	Approval of legislation and budgetary provisions. Development of software.	Early phase of implementation. Tax returns can be filed online, but the software allows only for a limited number of operations.	Level 4 + the software allows for credit/debit compensation when available in the country.	2
4.2.2.	Social security returns	Social security returns can not be filed online.	Government is considering proposals to allow for online filing of social security returns. Pilot project.	Approval of legislation and budgetary provisions. Development of software.	Early phase of implementation. Social security returns can be filed online, but the software allows only for a limited number of operations.	Level 4 + the software allows for credit/debit compensation when available in the country.	2

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
4.2.3.	Extension to other services (*i.e.* pensions, procurement, cadastre, etc.)	Other services cannot be filed online.	Government is considering proposals to allow for online filing of other services. Pilot project.	Approval of legislation and budgetary provisions. Development of software.	Early phase of implementation. Other services can be filed online, but the software allows only for a limited number of operations.	Level 4 + the software allows for credit/debit compensation when available in the country.	1
4.2.4.	Reporting on enterprise statistics	Reporting on enterprise statistics can not be filed online.	Government is considering proposals to allow for online reporting on enterprise statistics. Pilot project.	Approval of legislation and budgetary provisions. Development of software.	Early phase of implementation. Reporting on enterprise statistics can be filed online, but the software allows only for a limited number of operations.	Advanced phase of implementation + software allows for wide range of operations.	1
	E-government infrastructure						2
4.2.5.	Electronic signature (or equivalent)[8]	The government does not have a concrete plan on electronic signature.	Evaluation and formulation of detailed proposals of law on electronic signature and implementing regulations.	Approval of law on electronic signature and of the implementing regulations.	Solid evidence of implementation of law on electronic signature. Possibility to use e-signature in key areas for SMEs in contact with public administration.	Full implementation of law on electronic signature and full integration of electronic signature with other services of e-government. Regular reviews in consultation with SMEs.	2
4.2.6.	Connection between the databases of different public administrations, companies providing information only once, unless for updates	No connection between databases of different public institutions.	Government is considering proposals to enable connection of different public institutions.	The connection exists between some public institutions. Established connections enable data viewing.	The connection exists between all public institutions and data usage is allowed following special request by SME and/or institution.	The SMEs are not requested information which is already available in the database of another public administration (company registration office, tax administration, social security administration, labour authorities).	1
V)	***Adapt public policy tools to SME needs***						
5a.	**Support services for SMEs and start-ups**						
5a.1.	**SME support services**						3
5a.1.1.	Government action plan on business services	Provision of business support services to SMEs not included in the strategy (or equivalent).	Provision of business support services to SMEs mentionedin the strategy (or equivalent).	Level 2 + Business support services are associated with measures in the Action Plan.	Level 3 + Business support services are associated with measures in the Action Plan, targets, timeframe and expected impact.	Level 4 + mechanisms for monitoring the implementation in place	3
5a.1.2.	Range of business services	Very limited range of basic business services, available mainly through donor funded programmes.	More structured range of business service, available through a combination of public funded and private business providers.	Network of public funded business service providers. Good network of private business service providers, providing personalised services for enterprises.	Well developed market for business services, with good level of internal competition.	Level 4 + wide range of business services available in the country, including widespread presence of international consultancy firms.	2
5a.2.	**Business information for SMEs**						2
5a.2.1.	Business information	No basic information about starting and conducting a small business is made available from public sources.	Sporadic information about starting and conducting a small business is made available from a variety of unco-ordinated public sources.	Information about starting and conducting a small business is made available throughout the country by a number of official sources (business centres, chambers of commerce, etc.).	Extensive information about starting and conducting a small business is made available in paper form throughout the country. The location of the information is well advertised.	Level 4 + information about starting and conducting a small business are made available and well structured online.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
5a.2.2	Quality of online portal[9]	Existence of online portal unknown to SME community. Information is neither updated nor maintained.	Online portals are not easily accessible by the SME community. Portal is not user-friendly. Information is updated and maintained on an *ad hoc* basis.	There is one centralised portal for SMEs that redirects users to key websites for SMEs. Portal is regularly updated and maintained.	Level 3 + portal is user friendly and gathers the information related to SMEs from the different public authorities active in this field.	Level 4 + Portal includes the possibility for companies to communicate on rules and procedures which are considered to be disproportionate/and/or unnecessarily hinder SMEs.	1
5a.3.	**Support services for start-ups**						
5a.3.1.	Business incubators	No incubators in place and no plans to establish them.	Establishment of business incubators under discussion, local initiatives in preparation.	Detailed proposals and budget allocations in place, either at central or local government level. Pilot incubators in operation. Focus on job creation, no exit strategies.	Level 3 + several incubators in operation, out of the experimental phase. Provisions of basic services, some incubators used to foster innovation. Partial implementation of OECD guidelines on business incubators.	Level 4 + network of incubators throughout the country. Focus on innovation, provision of high quality services, and existence of exit strategies. OECD guidelines widely implemented.	1
5a.3.2.	Advisory support for start-ups	No advisory support in place and no plans to establish it.	Provision of advisory support for start-ups under consideration.	Pilot/small-scale projects of advisory support for start-ups in place.	Advisory support for start-ups well developed.	Level 4 + implemented throughout the country and monitoring mechanism in place.	1
5a.3.3.	Financial support for start-ups (vouchers, grants, etc.).	No financial support in place and no plans to establish it.	Provision of financial support for start-ups under consideration.	Pilot/small-scale projects of financial support for start-ups in place.	Level 3 + Financial support for start-ups well developed.	Level 4 + implemented throughout the country and monitoring mechanism in place.	1
5b.	**Public procurement**[10]						
5b.1.1.	Cutting tenders into lots	Cutting tenders into lots is not done, or it's done on *ad hoc* basis.	Pilot projects on cutting tenders into lots have been developed but there is not yet a consistent policy approach.	The possibility to divide contracts into lots is enshrined in legislation, but is subject to powerful derogations that make its implementation in practice rather weak.	The possibility to divide contracts into lots is enshrined in legislation and is commonly used.	The possibility to cut tenders into lots is largely used.	1
5b.1.2.	Information and publication of public procurement	Information on public procurement opportunities is scattered among variety of sources which makes it difficult for SMEs to follow about new opportunities.	Information on public procurement opportunities is centralised only at regional/local level.	Information on public procurement opportunities is centralised at national level.	Information on public procurement opportunities is centralised at national level and is free of charge.	Information on public procurement opportunities is centralised at national level and is free of charge. Helpdesks and trainings on procurement opportunities are offered to SMEs.	1
5b.1.3.	Penetration of eProcurement	Provision of basic information on tenders in electronic format (electronic contract notices, list of contractors, information on procurement activities, rules and processes, etc.).	Specific information for tender in electronic format (tender documentation in electronic format, downloadable forms and electronic tools for paper submission, but also more sophisticated searchable public tender databases, mail alerting systems, RSS feeds, etc.) – external communication.	Electronic forms, more or less no paperwork in the tendering process (electronic submission, electronic Q&A, e-awarding, etc.) – external communication.	Full electronic case handling without any paper-based formal procedure required (electronic communication throughout the procurement process, e-invoicing, etc.) – external and internal communication; systems connected to back-office and possibly to inter-agency processes.	Pro-active and automated communication, databases of reusable data (linking databases, e-attestation, full electronic contract management, etc.) – external and internal communication; systems integrated with back-office processes, inter-agency co-operation networks.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
5b.1.4.	Ensuring that payments are made on time	Late payments are not egulated.	There are efforts to combat late payments, but there is no consistent policy approach.	There is a law on late payments.	There is a law on late payments imposing strict deadlines for payments and penalties in case of non-compliance with these deadlines.	There is a law on late payments imposing strict deadlines for payments and penalties in case of non-compliance with these deadlines. The law is rigorously enforced.	1
5b.1.5.	Openness to foreign enterprises, either SMEs or large	The public procurement market is not open to foreign enterprises on the basis of open competition.	The public procurement market is open to foreign enterprises on the basis of open competition. The terms are fixed on a case by case basis.	The public procurement market is open to foreign enterprises on the basis of open competition. The terms are fixed in a limited number of bilateral agreements.	The country has opened small parts of its public markets, for instance on the basis of multilateral or a multitude of bilateral agreements.	The country is operating a transparent and competitive system and has opened significant parts of its public markets, for instance on the basis of multilateral or a multitude of bilateral agreements.	1
5b.1.6.	Setting proportionate qualification levels and financial requirements	There are no provisions to ensure the proportionate qualification levels and financial requirements.	Provisions to ensure the proportionate qualification levels and financial requirements are set only in guidance materials.	There are general provisions requiring the buyers to set proportionate qualification level and financial requirements.	There are specific provisions insuring that SMEs are not suffering from excessive requirements for qualification levels and financial requirements (such as turnover requirements, level of guarantee and deposits, qualification of staff, allowing grouping of economic operators, etc.).	There are specific provisions insuring that SMEs are not suffering from excessive requirements for qualification levels and financial requirements (such as turnover requirements, level of guarantee and deposits, qualification of staff, allowing grouping of economic operators, etc.) and there is evidence of implementation.	1
5b.1.7.	Allowing SMEs to bid jointly, *i.e.* to rely on the economic and financial standing and technical ability of other undertakings	The possibility for companies to bid jointly is not allowed.	The possibility for companies to bid jointly is allowed on *ad hoc* basis.	There are general provisions requiring the public authorities to give the possibility to companies to bid jointly.	There are general provisions requiring the public authorities to give the possibility to companies to bid jointly and there is evidence of implementation		1
VI)	***Facilitate SMEs' access to finance and develop a legal and business environment supportive to timely payments in commercial transactions***						
6.1.	**Sources of external finance for SMEs**						1
6.1.1.	Credit guarantee schemes	No credit guarantee scheme in place.	Credit guarantee scheme facility under consideration.	Credit guarantee facilities in place. (Government initiative and state controlled.)	Credit guarantee facility operating under contract to the private sector but state-funded.	Number of mutual or mixed credit guarantee schemes in place under private managers able to finance themselves out of fees alone.	1
6.1.2.	Public start-up funding	No public start-up funding facilities in the country.	Public start-up funding facilities exist at the level of pilot projects with limited impact.	Public start-up funding present throughout the country. Facilities mainly state or donor funded.	Public start-up funding facilities self-sustainable. Special facilities for targeted groups such as youth and women entrepreneurs.	Level 4 plus wide range of start-up funding products.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
6.1.3.	Business angels network	No business angel associations (seed capital funds) in the country; Little or no informal business angel activity.	Policy awareness; plans to encourage and foster business angel networks in drafting stage.	Pilot schemes to encourage and foster business angel networks implemented. Ministry of Economy/Finance has taken steps to promote or collaborate with business angel networks.	Level 3 + policy instruments piloted, including tax incentives for individuals engaged in seed-funding, operational expenditures subsidies, and promotion (*e.g.* business plan competition incl. prize money).	Level 4 + advanced support for business angels network, including use of tax incentives for capital gains to indentify high-net worth individuals; high-level promotion. Programmes are in place to enhance co-operation between angels and other investors. Potential use of public funds to enlarge business angels network's seed capital pool.	1
6.1.4.	Microfinance facilities (including credit unions)	No microcredit facilities (neither small credit lines nor microfinance sector) in the country.	Microcredit facilities (either small credit lines or microfinance) exist at the level of pilot projects with limited impact.	Microfinance sector present and operating throughout the country. Facilities mainly state or donor funded. Limited range of microfinance products.	Microfinance facilities self-sustainable. Special facilities for targeted groups such as youth and women entrepreneurs. Legal and regulatory framework for microfinance industry under preparation.	Level 4 + wide range of microfinance products. Appropriate legal and regulatory framework in place for microfinance.	1
6.1.5.	Leasing	No leasing activity, no plans for leasing law.	Leasing law under preparation.	Leasing law approved and institutional responsibilities clearly assigned. Some leasing activity.	Implementation of leasing law. Regulator active in monitoring market. Significant leasing activity.	Leasing law fully implemented. Regulation and supervision of the leasing sector is enacted. Significant leasing activity. Some specialised leasing companies.	1
6.1.6.	Availability of risk capital (*e.g.* venture capital, private equity funds)	No venture capital/private equity/ investment funds legislation under consideration.	Venture capital/private equity/ investment funds legislation under consideration.	Venture capital/private equity/ investment funds legislation in place.	Level 3 + several venture capital/ private equity funds investing, including funds specialised on SMEs, but the only exit possibility is direct sales.	Level 4 + range of exit options, including a functioning (second-tier) stock exchange with clear opportunities for initial public offerings (IPO) of venture-capital backed enterprises. Legislation in line with best practices.	1
6.1.7.	Access to stock market	Neither legal nor institutional framework in place for stock market.	Legal framework in place. Stock exchange in place with low market capitalisation (< 20% GDP). High concentration leading to low turnover (< 10%).	Stock exchange and legislation in place, but access limited to highly capitalised companies. Market capitalisation > 50% GDP. Market concentrated (10-20% turnover).	Level 3 + evidence of the enforcement of the legislation by securities exchange commission/ relevant authority. Possibility for listing either in the main market or in a market reserved for companies with lower capitalisation. Market not very concentrated (20-30% turnover).	Level 4 + fully enforced securities legislation, including the information disclosure requirements. Legislation in line with international standards. Active and well-functioning stock market for companies with lower capitalisation. Market capitalisation > 80% GDP, turnover 30-40%. Most capitalisation from private sector listed companies.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
6.2.	**Legal and regulatory framework**						3
6.2.1.	Cadastre	No functioning cadastres.	Plans have been made to implement a functioning cadastre.	Cadastre system in place, but the land ownership of the country has not yet been entirely documented.	The ownership of land has been documented but the cadastre is not fully functioning.	Level 4 + fully functioning cadastre allowing firms to use real estate as collateral in their efforts to access bank finance. Available online.	1
6.2.2.	Credit information services	No credit information services available in the country.	Credit information services in-place, but access limited to financial institutions.	Credit information services available to financial institutions and to the public. Both positive and negative credit information is available.	Level 3 + data on loans of more than USD 20 000 to legal and physical persons are collected and made available to financial institutions and the public upon request. Information is updated regularly and comprehensive.	Level 4 + more than 2 years of historical data are distributed. By law, borrowers have the right to access their data.	1
6.2.3.	Registration systems for moveable assets	No functioning registration systems for movable assets.	Legislation to establish a functioning registration system at the drafting stage.	Registration system of movable assets in place, but not yet fully operational. Information not easily accessible or fully reliable.	The ownership of pledges on the registered assets has been fully documented. Easy, low-cost access to registration and information.	Level 4 + fully functioning system for registration of movable assets, allowing firms to use movable assets as collateral in their efforts to access bank finance. Information available online.	1
6.2.4.	Collateral and provisioning requirements	Very high collateral requirements > 200%. Restrictive collateral definition and/or rigid provisioning requirements for uncollateralised loans.	Collateral requirement ranging 150-200% of loan amount. Restrictive collateral definition and/or rigid provisioning requirements for uncollateralised loans.	Flexible collateral definition and/or flexible provisioning requirements for loans under USD 30 000.	Flexible collateral definition and/or flexible provisioning requirements for loans under USD 30 000 and central collateral registry in place.	Flexible collateral definition and/or flexible provisioning requirements for loans under USD 30 000 and central collateral registry covering most bank loans.	1
6.2.5.	Creditor rights	There is no law on secured transactions.	Legal framework on secured transaction ensures two out of four rights listed below: 1) Secured creditors are able to seize their collateral after re-organisation, *i.e.* there is no "automatic stay". 2) Legislation provide restrictions such as creditor consent must be observed when a borrower files for reorganisation. 3) Secured creditors are paid first out of proceeds of liquidation of a bankrupt firm. 4) Management does not retain administration of property pending the resolution of re-organisation.	Legal framework on secured transaction ensures three out of four rights listed below: 1) Secured creditors are able to seize their collateral after re-organisation, *i.e.* there is no "automatic stay". 2) Legislation provide restrictions such as creditor consent must be observed when a borrower files for reorganisation. 3) Secured creditors are paid first out of proceeds of liquidation of a bankrupt firm. 4) Management does not retain administration of property pending the resolution of re-organisation.	Legal framework on secured transaction ensures all four rights listed below: 1) Secured creditors are able to seize their collateral after re-organisation, *i.e.* there is no "automatic stay". 2) Legislation provide restrictions such as creditor consent must be observed when a borrower files for reorganisation. 3) Secured creditors are paid first out of proceeds of liquidation of a bankrupt firm. 4) Management does not retain administration of property pending the resolution of re-organisation.	Level 4 + collateral enforcement is efficient.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
6.3.	**Other factors that affect demand and supply of finance**						
6.3.1.	Financial literacy	Financial literacy levels are extremely low in general. A national strategy encompassing a methodology to assess existing financial literacy levels and promote financial education programmes do not exist.	Financial literacy levels are extremely low among certain segments of the population. A national strategy encompassing a methodology to assess existing financial literacy levels and promote financial education programmes is considered.	Financial literacy levels are low and the lack of understanding of investment and savings products results in their underutilisation. A national strategy encompassing a methodology to assess existing financial literacy levels and promote financial education programmes exist.	Financial literacy levels low only with respect to certain complex products. Government schemes to rectify this gap exist. Consumers have access to a variety of credit and savings instruments provided by a range of entities, from online banks and brokerage firms to community based groups. Both information and training to consumers on the operation of markets and on the roles of market participants are available.	Consumers are educated on a wide range of financial products (investment, savings, etc.). Government support this effort by encouraging National campaigns to raise awareness of the population about the need to improve their understanding of financial risks and ways to protect against financial risks. Specific websites providing relevant, user-friendly financial information to the public exist. Media is widely used to achieve a wider coverage and exposure of relevant information and for the dissemination of education messages.	1
VII)	***Help SME to benefit more from the opportunities offered by the single market***						
7.1.1.	Technical regulations	No transposition of EU sectoral legislation in priority sectors.	Sectoral legislation in the priority sectors at the state of draft.	Sectoral legislation in place for at least part of the priority sectors.	Sectoral legislation in place and aligned with the acquis for all of the priority sectors.	Full implementation of the relevant sectoral legislation.	1
7.2.2.	Standardisation	No EU standards (ENs) adopted.	Adoption of ENs in priority sectors started (25% of ENs in priority sectors adopted) and upgrading of standardisation body in accordance with EU requirements started.	Adoption of ENs continued (50% of ENs in priority sectors adopted) and conflicting national standards abolished. Affiliate membership of standardisation body in CEN and CENELEC.	Adoption of ENs continued (80% of ENs in priority sectors adopted), conflicting national standards abolished and upgrading of standardisation body in accordance with EU requirements finalised. Application of membership to CEN and CENELEC.	Adoption of standards finalised (100% of ENs in priority sectors adopted), conflicting national standards abolished and full membership of national standardisation body in CEN, CENELEC, ETSI.	1
7.1.3.	Accreditation	No legislation aligned with the EU legislation (acquis) and no accreditation body exists.	Transposition of EU horizontal legislation started. Establishment and/or upgrading of accreditation body started.	Horizontal legislation on accreditation transposed and accreditation body in accordance with EU requirements set up. Membership in EA received.	Application of EA MLA signature status for some or all fields of accreditation. Accreditation body positively assessed by EA or by peer organisations.	Effective operation of the accreditation body. Signature status of EA MLAs.	1
7.1.4.	Conformity assessment	No legislation on conformity assessment aligned with the EU acquis exists.	Transposition of EU horizontal legislation on conformity assessment ongoing.	Upgrading of conformity assessment bodies in priority sectors in accordance with EU requirements ongoing. Existing national legislation on conformity assessment.	Conformity assessment bodies positively assessed by the national accreditation body. Designated and/or accredited CABs exist.	Legislation and institutional infrastructure as regards conformity assessment of products and designation of CABs operational. Existing operative CABs (or use of EU notified bodies) in ACAA sectors.	1

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
7.1.5.	Metrology	No legislation aligned with the EU acquis exists.	Transposition of EU legislation (*acquis*) on legal metrology started. Metrology strategy under way.	Continued upgrading of metrology body and/or institute in accordance with EU requirements.	Metrology body/institute recognised by relevant international/European organisations.	Effective operation of the metrological infrastructure. Legislation in place.	1
7.1.6.	Indicator Market surveillance	No legislation aligned with the EU acquis exists.	Market surveillance strategy drafted. Transposition of EU horizontal legislation adopted.	Organising a comprehensive market surveillance system in accordance with EU requirements underway.	Organisation of a comprehensive market surveillance system in accordance with EU requirements finalised. Necessary instruments (work plans, checks, customer complaints, accident statistics, risk analysis, etc.) started to be used.	Effective operation of the whole system.	1
7.1.7.	Administrative and regulatory information	No formal information or services provided for exporters or potential exporters to EU Single Market.	Some unco-ordinated information services available from ministries, chambers and other bodies.	State export promotion agency in place and developing co-ordinated information services on regulations and administrative procedures for exports to EU Single Market.	State export agency provides a range of information, at least in printed form, on main aspects of Single Market regulations, *e.g.* Single Administrative Documents (SADs), certificates of origin, health certificates, etc.	Integrated export promotion network with major focus on EU Single Market: Export promotion agency, commercial attaches, Chambers and Enterprise Europe Network offices providing full and up-to-date on-line information, including databases on Single Market regulations and procedures and member state requirements, *e.g.* language labelling.	1
7.1.8.	Sanitary and phytosanitary standards (SPS) – institutional framework	No national bodies in charge of SPS standards. Legislation significantly different from European/international standards.	Early adoption of legislative framework; beginning to set up national bodies in charge of SPS standards.	Further progress in adopting legislation and early implementation of legislative framework, national bodies have been set up; however still limitations (administrative or other issues).	National bodies well established, however with few limitations (administrative capacity or other issues). Still efforts needed to fully align legislation with European/ international standards.	National bodies very well established and functioning. Full alignment of legislation with European/ international standards.	1
VIII)	***Promote the upgrading of skills and all forms of innovation***						
8a.	**Enterprise Skills**						
8a.1.1.	Training needs analysis (TNA)	Small business TNA does not exist or is based on *ad hoc* surveys only. There is no regular and systematic collection of data on the training needs or training consumption in the small business community.	Government, social partners and business community are in dialogue with view to establishing a systematic TNA framework for the small business community.	A national TNA framework has been agreed between government, social partners, and business community with particular reference to economic growth sectors. The TNA framework identifies: *a)* skill weaknesses in the workforce; *b)* skill gaps; and *c)* future skill requirements. Standard data collection instruments and a data management system are in place as part of a wider national economic development plan.	TNA as defined by a life-long EL policy are undertaken in at least 20% of small businesses in growth sectors and reported publicly on a recognised website for access by enterprises, training providers and policy makers.[11]	Annual TNA is undertaken in at least 40% of small businesses in growth sectors and available publicly on a recognised website for access by enterprises, training providers and policy makers.[11]	3

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
8a.1.2.	Access to training[12]	No online public register of training providers and training programmes is available.	Register of training providers and training programmes broken down by regions, available on a recognised website.	Small business training provision is developed but is limited to specific towns and regions. Government support measures promote development of online training services.	Good training provider network developed across the country.[13] Evidence of online training services developing for small business community.	Good training provider network developed across the country. Data on online training acquire by enterprises is tracked by TNA system and evaluated as part of national entrepreneurship learning policy improvements.	1
8a.1.3.	Quality assurance[14]	There is no national framework for quality assurance of training delivered to the small business community. Some cases of accreditation of training programmes and training providers by international bodies.[16]	A range of *ad hoc* structures and tools[15] are being used to determine quality of training for the small enterprise community.	Dialogue ongoing between training providers, employers and government regarding quality, standards and accreditation of training provision for enterprises. This is linked to wider European quality assurance networks.	A national quality assurance system for enterprise training is agreed and is fully operational. Accredited training providers and programmes are posted on websites and information boards of small enterprise support agencies, public and private employment agencies and training centres.	The national quality assurance system for enterprise training[17] is operational and fully integrated in to European Quality Assurance Framework (trade skills) and recognised management training quality assurance systems.	2
8a.1.4.	Start-ups[18]	No training available for start-ups.	20% of newly registered start-ups in last 24 months have benefited from training and business advisory services in the reporting period including e-training).	40% of newly registered start-ups in last 24 months have benefited from training and business advisory services in the reporting period (including e-training).	60% of newly registered start-ups in last 24 months have benefited from training and business advisory services in the reporting period (including e-training). Business advisory services for small enterprises available up to 36 months after start-up.	80% of newly registered start-ups in last 24 months have benefited from training and business advisory services in the reporting period (including e-training). Business advisory services for small enterprises available up to 36 months after start-up.	1
8a.1.5.	Enterprise growth	No systematic approach to develop small enterprise human resources (knowledge and skills) for growing businesses.	Knowledge and skills development for enterprise growth has been agreed as a priority between business community and government and is registered in national economic development plan. Public finance agreed to support training and advisory services for growth enterprises.	Financial support for training and business advisory services for growing enterprises available.[19] Financial support is linked to clear criteria to allow enterprises to apply for subsidies to support training and advisory services linked to enterprise growth.	20% of growing businesses benefited from training and advisory services.	More than 50% of growing businesses benefited from training and advisory services.	1
8b	**Innovation**						
	Policy framework for innovation						3
8b.1.1.	Delegation of competencies and tasks	Measures concerning innovation policy are taken *ad hoc* by the concerned line ministries.	Government has completed a review and made plans for delegation of competencies and tasks concerning innovation policy. The plan has identified potential overlapping of tasks and inconsistencies in policy as well as possible synergies among programmes and institutions.	The organisational structure has been agreed and approved by the government. A clear map identifying responsibilities in innovation policy for each institution is established. Active measures to limit overlapping and to avoid major policy inconsistencies are in place (new programmes and schemes have to be reviewed by all concerned institutions and ministries).	A co-ordination body is in place (*e.g.* steering committee, inter-ministerial committee) and is chaired by a high political authority and supported by a well-structured secretariat, which ensures that policy exchange, co-ordination and consultation with stakeholders and civil society is carried out through previously agreed-upon mechanisms.	There is a sound system of programme co-operation on innovation policy among the institutions, aiming at integrating technological and non-technological activities, covering the full spectrum of innovation policy issues (including, development, application, absorption and diffusion). Wide-spread consultation with stakeholders.	2

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
8b.1.2.	Strategic approach to broad innovation policy	Innovation policy is not covered in any of the strategic documents covering enterprise policy, industrial policy, human capital development policies, or education and research policies.	Innovation strategy elements included in some of the previous mentioned documents, but no consistent approach, no indication of implementation actions.	Innovation policy developed and integrated into a number of strategic documents. Information on implementation plans, budget and time lines included in each of the documents. Strategic approaches are not co-ordinated.	Level 3 + strategic approaches are co-ordinated. Innovation programme/strategy is under implementation and adequately funded. Major components of the plan are active. Public-private partnerships (PPPs) projects being developed involving also universities and research centres.	Strategic approach to innovation is extensively implemented, including programmes covering the broad spectrum of technological and non-technological activities. Mechanisms in place to monitor the impact of the programme on company growth and direct/indirect spill-over's. Programme mostly based on PPPs projects, involving also universities and research centres.	3
	Support services for innovative companies						2
8b.1.3.	Establishment of innovation and technology centres	No networks, centres, or schemes to promote co-operation on innovation in place. Single, *ad hoc* initiatives in place	Pilot projects to establish innovation networks, centres or schemes to promote co-operation on innovation have been launched.	Action taken, specifically to promote the co-operation on innovation among enterprises, universities, and funded research centres. This promotion is publicly funded. Regulatory framework for PPP projects is in place.	Implementation of innovation promotion schemes. Innovation and technology centres in operation. Private/public partnership on national, regional, and local level in R&D, innovation and development.	Network of high level Innovation and technology centres present in the country. Strong relationship with research institutions and private sector at domestic and international level.	1
8b.1.4.	Innovation support services	No government or donor financed non-technological innovation support schemes (business plan, consultancy, etc.) in place to provide support to innovative companies.	Financial and technical support schemes introduced as pilot projects in place for a limited group of innovative companies.	Government supported schemes in place to co-finance services for innovative companies on a cost-sharing basis. Limited resources available and restricted range of business services covered.	Well-structured and budgeted schemes available to innovative companies. Wide range of services available on a cost-sharing basis. Services are available across the country.	Level 4 + schemes easily accessible and widely used by innovative enterprises and paid for in-full by the company. Impact of the schemes regularly monitored and evaluated. Proven track record of supporting the growth and development of innovative companies. Opportunities by improving quality management, bringing goods/services up to international standards, and in acquiring certification (if required).	2
8b.1.5.	Financial Support Services	No support scheme for innovative enterprises to determine financing options available for innovative projects.	Financial support service scheme under consideration and pilot project being launched, funded by government, donors and/or other organisations.	Financial support schemes are funded by government, donors and/or other organisations. Tailored services are provided to link innovative companies to sources of financing.	Financial support schemes are under implementation and adequately funded. Independent project evaluation system has been established. Co-operation with various financial institutions has been established to link innovative companies to sources of financing.	A complete chain of funding schemes is available for innovative projects, from grants, subsidies, seed funding to big venture capitals and loans. Project holders are well informed and aware of the availability of the funds through financial support schemes. There is evidence that a significant number of projects are funded every year.	3

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
IX)	***Enable SMEs to turn environmental challenges into opportunities***						
9.1.1.	The "greening" of the current strategies in the field of SMEs , industry and innovation	No reference is made in the policy framework to eco-efficient business and products or eco-innovation.	There are plans to include these elements in the new policy documents to be developed.	Eco-efficient business and eco-innovation are mentioned in the strategies in the field of SMEs, industry and innovation.	These elements are associated with concrete targets in Action Plans.	The strategy for SMEs promotes eco-efficient business and products, while the innovation strategy directs measures towards eco-innovation.	3
9.1.2.	Availability of expertise to SMEs on environmental issues	There is no information regarding this element and only commercial expertise is available.	The package on information regarding environmental issues and tools is under preparation.	Information regarding environmental issues and tools is available.	SME support organisations (chambers of commerce, local governments, NGOs, etc.) provide environmental support. This is not co-ordinated at national level and no specific funding is available.	There are specific programmes/ funding to provide expertise through SME support organisations with nationwide co-ordinated approach, contact points and information.	2
9.1.3.	Promoting the use of environmental management systems and standards	The use of environmental management systems (EMAS, ISO 14001, local systems) and standards is not promoted, and little known by business and public.		The government provides information on the EMSs to SMEs in the country, but no support measures ar in place for SMES to apply for certification.		There is specific funding and other incentives available for the implementation of EMSs and standards, information is widely available and it is integrated in procurement rules and on the market. Specific systems available for SMEs (like EMAS Easy).	2
X)	***Encourage and support SMEs to benefit from the growth markets***						
10.1.1.	Export promotion programmes	No export promotion programmes exist.	Export promotion programmes under consideration/some pilot programmes in place, limited funding available and no co-ordination between programmes.	New programmes approved. Programmes are largely funded by donor countries. Co-ordination between programmes. Basic trade information provided and some trade promotion activities (trade missions, country representation at major trade fairs) in place, but limited support given to a small number of SMEs.	Export promotion programmes are adequately funded but do not completely provide for all of the following: trade policy information and commercial intelligence, export promotion and marketing, trade fair participation, product development and financial services and training.	Range of well funded export promotion programmes capable of providing all of the dimensions mentioned in Level 4.	3
10.1.2.	Financial support for export promotion activities	No specific programme of financial support for export promotion activities exist	Programme of financial support for export promotion activities under preparation.	Programme of financial support for export promotion activities in place and under state control.	Independent programme of financial support for export promotion activities in place	Level 4 + collaboration with the banking sector for the granting of financial support for export promotion activities. Wide variety of options available.	3

		Level 1	Level 2	Level 3	Level 4	Level 5	Weights
10.1.3.	National SME promotion events	National SME promotion events occur on an *ad hoc* basis. Events are not open to the entire SME stakeholder community and cover a limited number of sectors.	National SME promotion events in under consideration by the government. Draft calendar of events being considered by concerned ministry/agency.	New national SME promotion events approved. Evidence that relevant stakeholders have been informed of and invited to upcoming events.	Regular hosting of national SME promotion events occur. Evidence that a wide representation of stakeholders attend and that events cover a wide range of sectors.	Level 4 + evidence that national SME promotion events have enhanced SME competitiveness. Regular evaluation of past events and planning of future events held by relevant ministry/agency.	1

1. Note that this indicator applies to lifelong entrepreneurial learning and is cumulative *i.e.* each ranking requires fulfilment of the earlier levels of the indicator.
2. This indicator is about promoting entrepreneurship as key competence, so, it prompts the governments to consider the value of introducing entrepreneurship in the national curricula as a key competence and implementation in the practice of teaching in upper secondary schools, so, it is also important to estimate how many schools have introduced the subject.
3. Government includes ministries responsible for fiscal, economic, employment, social and education and training policies. Stakeholders include Chambers of Economy, employers' organisations, trade unions, civic interest groups.
4. The term "data" means here any type of "evidence": administrative statistics, other quantitative data, analysis, reports, texts of laws and regulations, etc.
5. Policies to support Female Entrepreneurship under this indicator stimulate a closer look on the role and contribution of women entrepreneurs into the national economic growth, rather than at the aspects of gender equity or at the social aspects of ensuring equal opportunities for men and women to participate in business.
6. "Strategy" refers to any official document guiding SME and enterprise policy action.
7. *http://ec.europa.eu/enterprise/policies/sme/small-business-act/sme-test/index_en.htm.*
8. "Or equivalent" refers to alternative methods of validating government business communication.
9. Portal = A website considered as an entry point to other websites, often by being or providing access to a search engine. Ex: *http://ec.europa.eu/small-business/index_en.htm*.
10. *http://ec.europa.eu/enterprise/policies/sme/business-environment/public-procurement/index_en.htm.*
11. Evidence for this indicator will be taken from enterprise survey-based data.
12. This indicator evaluates availability of training services for small enterprises.
13. Information on training providers available within economic development departments of local/regional administration offices.
14. Reference is made here to accreditation as only one of the elements of the training quality assurance system: Government, private institutions, training providers and their clients, etc. all could have a role in quality assurance.
15. Various types of public and/or private accreditation.
16. For example, sector-based quality focus-groups, pilot actions for training standards, employer satisfaction surveys.
17. This indicator refers to a quality assurance system for enterprise training (for the development of both sectoral and management skills) that would have a national scope and go in-line with the key European principles of quality assurance.
18. Start-up training comprises management, basic finance and basic marketing skills supported by public and/or private funds.
19. Financial support will particularly address the knowledge and capacities related to the EU regulatory framework.

ANNEX B

Declaration on fostering SMEs, entrepreneurship and competitiveness in Eastern Europe and the South Caucasus (17 June 2011)

At the *Second Ministerial Roundtable of the OECD Eastern Europe and South Caucasus Initiative*, held in Prague, the Czech Republic, on 17 June 2011, government delegates in the Roundtable adopted *The Declaration on Fostering SMEs, Entrepreneurship and Competitiveness in Eastern Europe and the South Caucasus (covering the Eastern Partnership countries)* (Annex).

Small and medium-sized enterprises (SMEs) are a key driver of economic growth and employment in both emerging and developed economies. They constitute a major source of knowledge, skills, and innovation, and are an important source of employment. SMEs in Eastern Europe and the South Caucasus are playing an increasingly important role in the transition to vibrant and market-driven economies in which entrepreneurship can thrive. Efforts to foster growth in SMEs should address key policy dimensions affecting the business climate, and identify key constraints affecting the ability of firms to produce, invest, and grow.

Governments of the Eastern Europe and South Caucasus countries are becoming increasingly aware of the need to develop policies that create a level playing field for SMEs through regulatory reform and the removal of administrative burdens. The following Declaration re-affirms the principles instrumental to fostering innovation, employment and entrepreneurship through continued expansion and development of SMEs, entrepreneurship and competitiveness in the Eastern Europe and South Caucasus economies.

Declaration on fostering SMEs, entrepreneurship and competitiveness in Eastern Europe and the South Caucasus

We, the Ministers and government representatives of countries participating in the OECD Eastern Europe and South Caucasus Initiative, assembled in Prague, the Czech Republic, on 17 June 2011 for the *OECD Ministerial Roundtable on Enterprise and Competitiveness Policies*,

Recognising

- That SMEs are a key driver of economic growth, innovation and entrepreneurship in OECD member countries and non-OECD economies.

- That SMEs in the Eastern Europe and South Caucasus countries represent an untapped reservoir for job creation, economic growth and social cohesion.
- That a targeted and integrated support approach is required to accelerate the rate at which entrepreneurs in the Eastern Europe and South Caucasus countries are starting new businesses, growing their enterprises, creating employment, and participating fully in economic development activity.

Recalling

- The adoption by Ministers of almost 50 OECD member countries and non-OECD economies of the "*Bologna Charter on SME Policies*" in June 2000, which emphasised the important contribution of SMEs to economic development and social cohesion.
- "*The Istanbul Ministerial Declaration on Fostering the Growth of Innovative and Internationally Competitive SMEs*" adopted in June 2004, where Ministers of 73 OECD member countries and non-OECD economies noted that SMEs "constitute an important dynamic element in all economies", and "play a key role in driving sustainable economic growth and job creation while contributing to the social, cultural and environmental capital of nations".
- The Ministerial Conference on "*Investment and Competitiveness in South Caucasus and Ukraine*" of April 2009, which recognised that fostering the growth and development of SMEs is an effective strategy for improving the business climate, attracting foreign investors and trigger sustainable economic development and social progress.
- The "*Bologna+10 High-Level Meeting*", which further highlighted the need to develop and evaluate SME support policies in the wake of the 2008-09 financial crisis.
- The Joint Declaration of the Prague Eastern Partnership Summit of May 2009 on "New Association Agreements, beyond existing opportunities for trade and investment" and the invitation addressed to major international financial institutions to "to establish an appropriate joint small and medium-sized enterprise facility".

Acknowledging

- The recent work of the OECD Eurasia Competitiveness Programme, including the Enterprise Policy Performance Assessment of the Eastern Partnership countries and its work on fostering SMEs, entrepreneurship and competitiveness in the Eastern Europe and South Caucasus through policy dialogue on:
  - Access to Finance.
  - Human Capital Development.
  - Investment Policy and Promotion.
- The main findings of the OECD Eastern Europe and South Caucasus Competitiveness Outlook highlighting the region's competitive advantages and identifying barriers that need to be dismantled for its economies to reach their full potential, specifically by:
  - Improving access to finance for SMEs by further pursuing reforms to improve the institutional framework for microfinancing and by introducing targeted instruments, for example such as guarantee schemes, to enhance bank lending to SMEs.
  - Promoting the development of skills that match labour market requirements, and mobilising the full competitiveness potential of an already strong human capital base by further improving efficiency of spending as well as quality and relevance of education.

- Further reforming investment policy frameworks, including better protecting investors through more transparent and non-discriminatory legal proceedings, and further building investment promotion capabilities linked to industrial policy objectives.

Welcoming

- The support provided by the OECD Eastern Europe and South Caucasus Initiative in collaboration with the European Commission, the European Bank for Reconstruction and Development (EBRD) and the European Training Foundation (ETF) within the framework of a joint assessment to identify policy barriers for SMEs and SME growth opportunities. This joint assessment aims at enhancing investment, competitiveness and private sector development in the Eastern Europe and South Caucasus countries through the following key areas:
  - Co-operation and co-ordination between Eastern Europe and South Caucasus countries on the evaluation of SME policy development and SME support schemes.
  - Establishment of a new Eastern Partnership Enterprise Policy Development Working Group to contribute to policy evaluation and the preparation of recommendations for improvements to SME policy in participating countries.
  - Preparation of an *Enterprise Policy Performance Assessment of the Eastern Partnership Countries*.

Reaffirming

- The need for an institutional framework that will contribute to a business environment that is conducive to entrepreneurship and facilitates entry, growth, transfer of ownership and smooth exit of enterprises.

Agree to develop targeted policies to support SMEs and entrepreneurship in the Eastern Europe and South Caucasus countries, based on the guiding principles of the EU Small Business Act, by:

- Creating an environment in which entrepreneurs and family businesses can thrive and entrepreneurship is rewarded.
- Ensuring that honest entrepreneurs who have faced bankruptcy quickly get a second chance.
- Designing rules according to the "Think Small First" principle.
- Making public administrations responsive to SME needs.
- Adapting public policy tools to SME needs.
- Facilitating SME access to finance and developing a legal and business environment supportive to timely payments in commercial transactions.
- Helping SMEs to benefit more from the opportunities offered by the Single Market.
- Promoting the upgrading of skills and all forms of innovation.
- Enabling SMEs to turn environmental challenges into opportunities.
- Encouraging and supporting SMEs to benefit from the growth of markets.

Invite the OECD, its member countries and other international organisations to:

- Give high priority in their development programmes to promoting SMEs and entrepreneurship and enhancing participation in the economy.

- Develop tools to improve information and understanding of the current situation of SMEs in the Eastern Europe and South Caucasus countries.
- Provide support to regional and national initiatives by Eastern Europe and South Caucasus countries to research, training and advocacy activities.
- Implement policy seminars designed to focus on policy dialogue, peer review and capacity building and support the design and implementation of targeted policies for SMEs and entrepreneurship.
- Set up policy working groups at the country level to support public-private policy dialogue and the exchange of best practices on innovation and SME competitiveness.
- Facilitate the exchange of best practices with Eastern Europe and South Caucasus countries on fostering SMEs, entrepreneurship and innovation.

Confirm the work programme for 2011-12 proposed at the *Ministerial Roundtable* discussions on 17 June 2011 and our participation in all the activities outlined therein.

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

The OECD is a unique forum where governments work together to address the economic, social and environmental challenges of globalisation. The OECD is also at the forefront of efforts to understand and to help governments respond to new developments and concerns, such as corporate governance, the information economy and the challenges of an ageing population. The Organisation provides a setting where governments can compare policy experiences, seek answers to common problems, identify good practice and work to co-ordinate domestic and international policies.

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EUROPEAN COMMISSION

The Directorate-General for Enterprise and Industry of the European Commission works to ensure that EU policies contribute to the sustainable competitiveness of EU enterprises and facilitate job creation and sustainable economic growth. It plays a major role in implementing the Europe 2020 strategy for growth and jobs.

EUROPEAN TRAINING FOUNDATION

The European Training Foundation (ETF) helps transition and developing countries to harness the potential of their human capital through the reform of education, training and labour market systems in the context of the EU's external relations policies.

EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT

The EBRD is an international financial institution that supports projects from central Europe to central Asia. Investing primarily in private sector clients whose needs cannot be fully met by the market, the Bank fosters transition towards open and democratic market economies.

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SME Policy Index

Eastern Partner Countries 2012

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Annex 1. Small Business Act assessment framework

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