

SMEs are Facing with Recession Trends

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Abstract: In 2014, in spite of some signals of recovery in the previous year, the recession trends in SME development prevailed again. It was outcome of severe water flood, low external demand related to EU recession, low domestic demand, imposed by measures of fiscal consolidation program and general, not favorable business environment. Decreasing number of new established companies and at the same time increasing number of those closed one continued. As small and opened economy, Serbia is oriented toward foreign trade, but SMEs are still not very competitive abroad, considering their share in overall volume of export and import, lower than 1/2 of total. As positive trend one can see increase in volume of export, faster than increase in import. Several investigations of quality of business environment proved not favorable position of SMEs with important limits of development, regarding financial problem, like collecting of claims and access to financial sources, and complicated and expensive administration. Those findings are very similar to opinion collected by interviewing of entrepreneurs, which pointed limits for investments and development of business. Difficult measures of fiscal consolidation, which are introduced in order to put public debt under control, are combined with introduction of the strategy for SME support. So, one can expect that those measures would result in more friendly business environment for SMEs, but need time to be materialized in greater number of new companies and increasing competitiveness on the international market.

Keywords: SME, crisis, business climate, support policy

1 Introduction

If one can conclude that there were modest and fragile signs of recovery of Serbian SME in 2013[1], than, for 2014 this statement cannot be drawn. It means that, unfortunately, SMEE are still in recession.

Why we cope with SMEE at all? They count 99,8% of all economic subjects and create 30% of the national GDP[2].After 15 years of transition the state is taking care about large companies, pretty unsuccessfully. More than 180 large companies

were closed at the end of 2014, which could not survive and moreover, foreign creditors, IMF and WB mainly, asked for it, arguing that the Government has to cut subsidies, as a part of fiscal consolidation program.

After positive, although weak and unsecure trends in business demography, we are in 2014 witnesses of declining number of companies. Shops, at the same time, somewhat increased their number, but it cannot give overall positive remark for SMEE. The main factors of recession are related to 1) overall unfavorable business conditions, due to water flood in May of a catastrophic character and 2) fiscal adjustment program, which included cut in aggregate demand (cut in wages of public sector, pensions and dismantle subsidies to large state owned companies). The outcome was decrease of 1,5% in GDP¹.

Foreign trade is important factor of development and, at the same time, gives us relevant information whether our companies are competitive abroad or not. Although SME's share in total export is 98% [2], accounting to numbers, they contributed in 2013 with 43% of value of total export. Large companies are simply more important.

The main Serbian economic and not only economic problem is high unemployment rate, which reached 17% in 2014¹. At the beginning of the recession SME did not reacted by cutting number of jobs. However, in last few years they did it in order to accommodate to difficult conditions. Slower recovery of SME in comparison to large companies induced cut in number of employees by 17%, while in large one decrease of number of jobs was 0,5% only[2].

When asked what are limits for recovery and development Serbian entrepreneurs pointed pure access to finance (57%), claims collection (53%), low demand (42%) and low competitiveness (33%) [3].

National Alliance for Local Economic Development, NALED, has prepared the analysis of business environment, counted RIS, Regulatory index of Serbia [4]. Overall remark was slightly better than year earlier, which impose better business environment, but one can say that speeding up reforms needs time to be matured and even more time to give positive economic performances as result.

2 Business demography

Statistical data on business demography are structural indicators which can be used to assess improvement in development of SMEE, assess dynamism of creating of economic subjects and new jobs and increase in number of SME and shops. As a negative outcome of economic crisis and worsening business environment, from

¹RSO - Statistical Office of RS

2008 on number of new established companies and shops is decreasing, while at the same time number of those which close their activities is increasing.

In 2013 number of newly established companies was somewhat increased (0,2%), while number of closed companies was cut by 2/3 (Table 1). At the same time number of new shops was higher (3,1%) and closed one increased, as well (9,8%). It was encouraging to conclude that there are sign of unsecured recovery [1].

Unfortunately, those positive signals were not long lasting, as oscillations continued. Namely, in 2014 unfortunately number of newly established companies decreased in comparison to the year earlier (-4,6%), while number of closed companies decreased also, but less (-1,4%), with negative net effect. At the same time number of new and closed shops decreased (-6,6% and even -24,8%, respectively) (Table 1).

If one can look at net effect, than can be satisfied, as number of companies, although modest, is increasing from year to year, after reverse effect in 2011, and in 2014 was 3,2:1, while for shops net effect was almost zero (1,1:1).

	No of enterprises		No of shops		Net effect	
	opened	closed	opened	closed	companies	shops
2008	11.248	3.068	43.375	34.572	3,7	1,3
2010	9.461	9.325	35.036	37.086	1,0	0,9
2011	8.470	13.581	32.236	35.288	0,6	0,9
2012	8.648	7.355	30.200	32.853	1,2	0,9
2013	8.735	2.562	30.931	36.379	3,4	0,9
2014	8.266	2.592	29.102	27.137	3,2	1,1

Table 1

Serbia - The number of newly established and closed SME

Source: RSO1, processed by PPS3 - authors' research

Looking at macroeconomic circumstances on the domestic market we can conclude that in 2014 business conditions were less favorable than the year earlier. GDP was less for 1,5% in comparison to 2013¹, in spite of projection of modest increase of 1%. This drop was due to water flood in May, of catastrophic character, which hampered mining and energy production, due to modest demand and recovery in EU, as the main Serbian international trade partner, and due to suppressed domestic demand, induced by introduction of a fiscal adjustment program, which imposed

³-PPS – Public Policy Secretariat of the Republic of Serbia

cut in wages in public sector, pensions also and cut in subsidies to companies in restructuring process.

The continuation of recession (Serbia is facing zero rate of growth of GDP for six year during the crisis)¹, decreasing foreign and domestic demand, decrease in investments, increase in risks and operating costs and fear of failure, altogether negatively affected business environment. Decreasing number of newcomers in SMEE sector affected limits for new jobs and increase in productivity, which is vital factor for improvement of international competitiveness. For instance, during 2014 number of newly established companies was 3.114 per month, while during 2013 was 3.200 and even 5.000 in 2007, the last year prior to the crisis.

	Enterprises		Sole traders		Total	
	birth rate	death rate	birth rate	death rate	birth rate	death rate
2007	16,2	5,0	22,6	14,9	20,7	12,1
2009	11,3	4,1	17,4	16,1	15,7	12,7
2010	10,7	10,5	15,6	16,6	14,0	14,6
2011	9,3	15,0	14,1	15,4	12,7	15,3
2012	9,4	8,0	13,4	14,5	12,2	12,6
2013	7,9	2,3	14,5	17,1	12,3	12,0

Table 2
 Serbia - Birth and death rate of enterprises and sole traders
 Source: RSO1, processed by PPS2 - research

Better look at the business demography one can get if count so – called birth rate, which calculate number of new established companies / shops as percentage (share) in total number of active companies (shops) and death rate, which calculate number of closed companies / shops in total number of active (Table 2). The tendencies are clearly negative, as consequence of several factors, as explained earlier.

On average, in 2013, on each one thousand inhabitants in Serbia operated 44,1 SMEE (so - called density of SMEE), of which 5,5 were new established economic subjects. If look at active population, of age between 15 and 64 years old, than on each one thousands inhabitants 64,1 SMEE operated, of which 8 new established. According to density of SMEE Serbia in 2013 was on EU average with 44,1 (EU 41), where Chess Republic reached the highest coefficient (90,2) and the least Romania (26,6) [5].

The rate of survival is indicator which points how many small and medium companies and shops established during the year succeed to survive in the year n+2,

when one can suppose that certain economic subject is adjusted to economic circumstances and found its own niche on the market. Comparing the indicator in 2007 and 2013 one can conclude that 62% of new comers survived during the first two years and continued to operate and also that the rate was much higher in 2007 than in 2013. The higher rate of survival had companies (93%) than shops (55%).

3 Regulatory index

National Alliance for Local Economic Development, NALED at the end of 2012 for the first time prepared the analysis of business environment quality, called Regulatory index of Serbia, RIS. The purpose of this investigation is to calculate quantitative, overall index of transparency and quality of legal process, law implementation, competitiveness and predictability of business environment.

Final remark for 2014 of RIS is 41,8 of maximal value of 100 points, which means that quality of regulatory framework in Serbia is 41,8 % of desirable standard. Although there is evident improvement in performances of the Government and other institutions measured by increase of 10 points in comparison to the previous year (RIS in 2013 was 31%) low value of the index points that quality of legal framework and its implementation is still a bottleneck for establishment and development of business [4]. Moreover, even when business environment is improved one has to wait years to see results in increasing number of companies and shops and their development.

Investors and entrepreneurs are looking for stabile economic policy, legal security, cheaper and more efficient administration and more transparent communication with civil services. From this point of view business environment is still non – favorable. Access to information is single component of the complex index which is improving from year to year. Administrative costs are still high and there is lack of cost – benefit analysis of laws, prior to their approval in the Parliament. Public discussions are organized rarely, for 1/3 of all law proposals and even 2/3 of law passed procedure as urgent matter [4].

Component	Indicator	2013		2014	
		Mark	Total	Mark	Total
Quality and thoroughness of law preparation	Effect analysis	63,6	43,0	51,4	39,6
	Quality of effect analysis	52,4		52,4	
	Regulatory effect quantification	12,9		15,0	
Publicity of law preparation	Public discussion	36,3	30,5	72,3	49,4
	Access to law proposals	-		63,8	
	Urgent procedure	19,2		27,2	
Legal predictability	Compliance of plan	-	-	21,9	41,7
	Frequency of changings	-		61,6	
Regular problem overcoming	Gray book acceptance	20,4	184	-	-
	SRP acceptance	16,7		-	
Accuracy in law implementation	Approval of sub - law	18,2	10,3	22,0	12,6
	Late in approval	2,4		3,1	
Regular and para-fiscal duties	Administrative costs	33,3	25,4	40,0	29,7
	Para-fiscal duties/budget rev.	17,5		18,6	
Access to information	Speed of admin answer	11,1	62,6	55,5	77,7
	Access to public info	76,7		77,7	
	Web cites content	100		100	
Regulatory index of Serbia			31,7		41,8

Table 3
 Regulatory index Serbia
 Source: [4]

The first component of RIS is related to assessment⁴ of the quality of law proposals, firstly, answers whether law proposal is based on the cost - benefit analysis of effects, secondly, what is the content of the analysis prepared, and thirdly, whether the analysis were prepared with quantification or not. As can be seen, unfortunately there was decrease in mark of quality of law preparation.

The second component answers the question about the degree of public discussion of legal proposals. Generally speaking, there is common feeling that public is consulted about law proposal from time to time, and more important, there are too many laws passed through urgent procedure, which means without any consultation. It is encouraging fact that there is improvement in all aspects of publicity of law proposals.

The third component is newly introduced one. It is related to stability of legal framework, which is very important issue for investors and entrepreneurs. The first indicator is measuring what is the degree of fulfillment of plan of legal changes. As one can see from the table it is clear that the Government succeed to introduce only 1/3 of legal changes promised. The second one is measuring frequency of legal changes and according to the result 30 laws was changed even 98 times, which says that there is low level stability of legal framework.

The fourth aspect is related to accuracy of legal implementation, measuring whether laws are prepared for implementation by sub – law acts approval. One can see that this aspect is a weak point, as the share of imposed sub – laws act in total is very low and postponing of sub – laws act approval and their late implementation is often.

The fifth aspect is very important one, especially important for entrepreneurs. It is related to fiscal and other related duties. According to the investigation there is slight improvement in the tax procedure and its costs, although low level of the mark says that there is a lot of room for improvement, which means that tax duties are still too high.

The last component of RIS is related to access of information. According to the assessment there is improvement in comparison to the previous year and more important, one can see relatively high level of mark.

⁴ Office for Regulatory Reform and Regulatory Impact Assessment (now PPS)

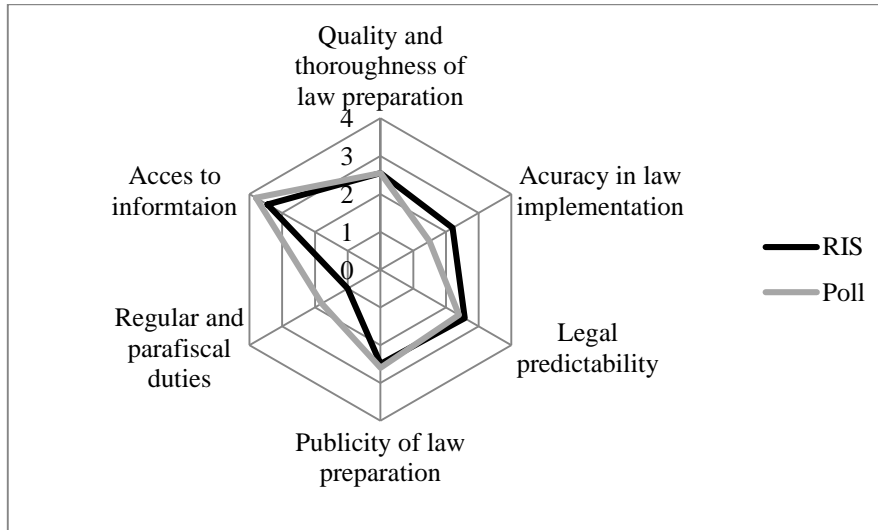


Figure 1
 Regulatory index of Serbia and Poll
 Source: [4]

In order to double check the findings, the same analysis included investigation prepared by IPSOS Strategic Marketing about entrepreneurial perception on legal framework for business (Figure 1). According to their opinion the best aspect of the legal framework in Serbia is related to access to information about legal framework on web sites of ministries and other institutions (57% positive). The worst point of legal framework for business is related to speed of reaction of the Government on entrepreneurial complaints and introduction of legal adjustments necessary (2% positive, only) [4].

When asked about bottlenecks of busies development the most entrepreneurs pointed operation of their competitors in shadow economy (67% of them), than high tax and other duties on wages (64%), thirdly, other tax and administrative duties (55%). The least problematic, from the point of view of entrepreneurs, are limits related to custom duties (20% of them pointed it as a problem), receiving license for work (27%) and different inspections (28%).

The poll investigation covered also question of administrative procedure and their time consuming as problem for business development. Procedure for getting construction license was labeled as the worst procedure (for 16% of all entrepreneurs asked). The second was procedure within tax office (10%), thirdly, court procedure (10%). The least problematic for entrepreneurs are administrative bills procedure (0,4%), traffic permit (0,4) and VAT payment procedure (0,8%).

4 Competitiveness problem still persists

For small and opened economy, like Serbian, foreign trade is important factor for development and recovery in order to overcome the economic crisis. Export and import volume and their structure point efficiency of companies, including SMEs and say whether our companies are competitive world wide or not. In order to improve competitiveness National Bank of Serbia introduced policy of flexible exchange rate of domestic currency (dinar), with intervention on the FX market, like Romania and Hungary, with idea to make Serbian export competitive in price term.

Considering the share of SMEs in total export volume one can be satisfied considering number of exporters, as SMEs in 2013 reached 98% of total number of exporters, but cannot be satisfied with more important indicator - value of export, as SMEs share was 43% only, which points simply that large companies are more important [2]. As it was noted earlier the recession effects of the crisis are the most recognizable in SME sector. Gross Value Added (GVA), employment and productivity of those were in 2013 still below level from 2007.

In 2013 SMEs succeed to export 4,6 billion € and import 8,3 billion €, with trade deficit of 3,7 billion €. There are some positive points in foreign trade. Number of exporter increased by 3,9%, while number of importer increased by 1,6%. One can recognize continuity of the trend of increasing covering value of import by value of exports for SMEs from 36,5% in 2007, 52,3% in 2011, 51,3% in 2012 and finally 55,3% in 2013[2].

The analysis of foreign trade of SMEs according to scale of companies: micro, small and medium, gives us interesting results. The medium scale companies were in 2013 the most powerful, covering 48% of total SMEs exports and 40% of total imports, while micro and small companies were on the similar level. Out of total foreign trade deficit 3,7 billion €, small scale companies were segment with highest deficit 1,7 billion €, than medium companies 1,1 billion € and micro companies 0,8 billion €.

Those not very favorable findings regarding low competitiveness are additionally proved by GEDI, Global Entrepreneurship Development Index. It is indicator of quality of entrepreneurship related to their effects and innovations, induced by individual and institutional factors. It is covering three dimensions of entrepreneurship: firstly, entrepreneur attitude, related to public opinion about entrepreneurship; secondly, entrepreneurial activities, measuring activities with potentials for speedy development and thirdly, entrepreneurial intentions, pointing entrepreneurial intentions to invest and introduce new products and technologies [6].

Overall value of GEDI for Serbia in 2013 was 0,20, with 80-81st rank. It is unfortunately the lowest value of overall GEDI indicator within the Region, beside

Bosnia and Herzegovina. Within the group of countries, which development is efficiency induced, Serbia was the last one, while the highest rank had Montenegro (0,32). All three dimensions were not favorable, which again points not favorable business environment and slow recovery of the national economy [6].

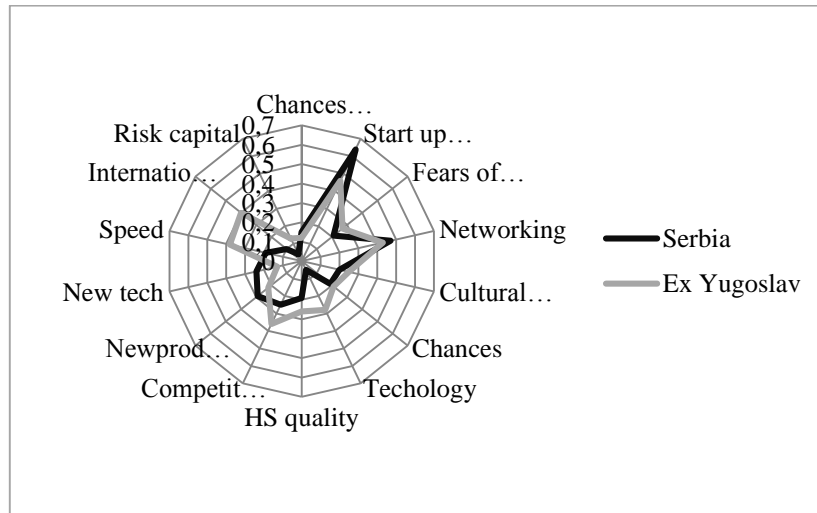


Figure 2
 GEDI – Serbia and Ex - Yugoslav countries
 Source: [6]

If compare to countries with similar level of development, countries in transition, Serbia has a comparative advantage in skills of those who start business and in introduction of new products and technologies. If talk about weaknesses one can point a few chances for start - ups, low share of those new firms with medium and high technologies, low quality of human sources, level of competition, potential for speedy development and use of risk capital and lastly, low level of internationalization of SME.

Generally speaking, level of entrepreneurship development, considering GEDI index, increased so little during the crisis, from 0,18 in 2008 to 0,2 in 2013. Those findings ask for new development model of the national economy, in which development of so - called dynamic entrepreneurship has to be recognized as especially important.

5 New Strategy for SMEs development support

At the end of 2014 the draft Strategy for support of Small and medium scale enterprises and entrepreneurship and competitiveness in the period 2015-2020(the Strategy in text followed), together with the Action plan for its implementation were prepared. The Strategy⁵ defined framework, goals, priorities and measures for development of micro, small and medium scale companies and entrepreneurship in the medium term. It is also part of strategic framework for development of competitiveness of RS and it is complement with previously enacted documents in this filed, mainly the Strategy of industrial development in the period 2011-2020. It is important to note that those principals from EU supporting policy for SME development, Europe 2020 and Small Companies Act, were implemented.

The main goals of the Strategy are as follows: improvement in business environment, improvement in access to financial sources, development of human resources, strengthening of sustainability and competitiveness of SME, access to new market and development and promotion of entrepreneurship. It is very important point that Ministry of Economy would develop the system for monitoring of its implementation, which was usual weakness of development documents in the past. Also important point is a plan to execute the first detailed ex - post analysis of implementation of the Strategy after two years period.

6 Conclusion

Serbian economy is facing zero growth rates, during the last six years of crisis. SMEs are still in recession, because they are severely hampered with lower demand from EU, lower domestic demand related to implementation of fiscal consolidation program, worsened business environment and facing low competitiveness on the Global market. Business demography continued a trend of decreasing number of new established companies and shops. Entrepreneurs are oriented to survive mainly and not to invest into development. They are faced with strong development limits related mainly to financial problems, like claims collection and difficult access to finance and less, to low demand (externally and internally) and complicated and high administrative and fiscal duties. Different investigations prepared to measure achievements in entrepreneurship, like Regulatory Index of Serbia and GEDI, pointed out similar problems. It is encouraging that Government has speed up market reform and at the same time defined the Strategy for SMEs support, as a

⁵ The draft Strategy for support of Small and medium scale enterprises and entrepreneurship and competitiveness in the period 2015-2020 (<http://www.rsjp.gov.rs/s/Mi%20A1ljenje-na-Predlog-strategije-za-podr%20A1-raz-malih-i-sred-preduz-preduz-i-konk-2015-2020/50>)

general framework for entrepreneurial support in the future. However, those difficult and important steps need time to be introduced and even more to produce results.

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