







**LATVIJAS  
BIZNESA  
SAVIENĪBA**

# **SUPPORTING GROWTH OF SMEs IN THE REGIONS**

## **RECOMMENDATIONS**



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Authors:

Gunta Misane, Eduards Filippovs (Latvia)

Nino Elizbarashvili (Georgia)

Ilqar Huseynli (Azerbaijan)

Yurii Vdovenko (Ukraine)

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Social Strategic Researches and Analytical Investigations Public Union (Azerbaijan)

Georgian association “Women in Business”

Business Union of Latvia

Center for cross-border cooperation (Ukraine)

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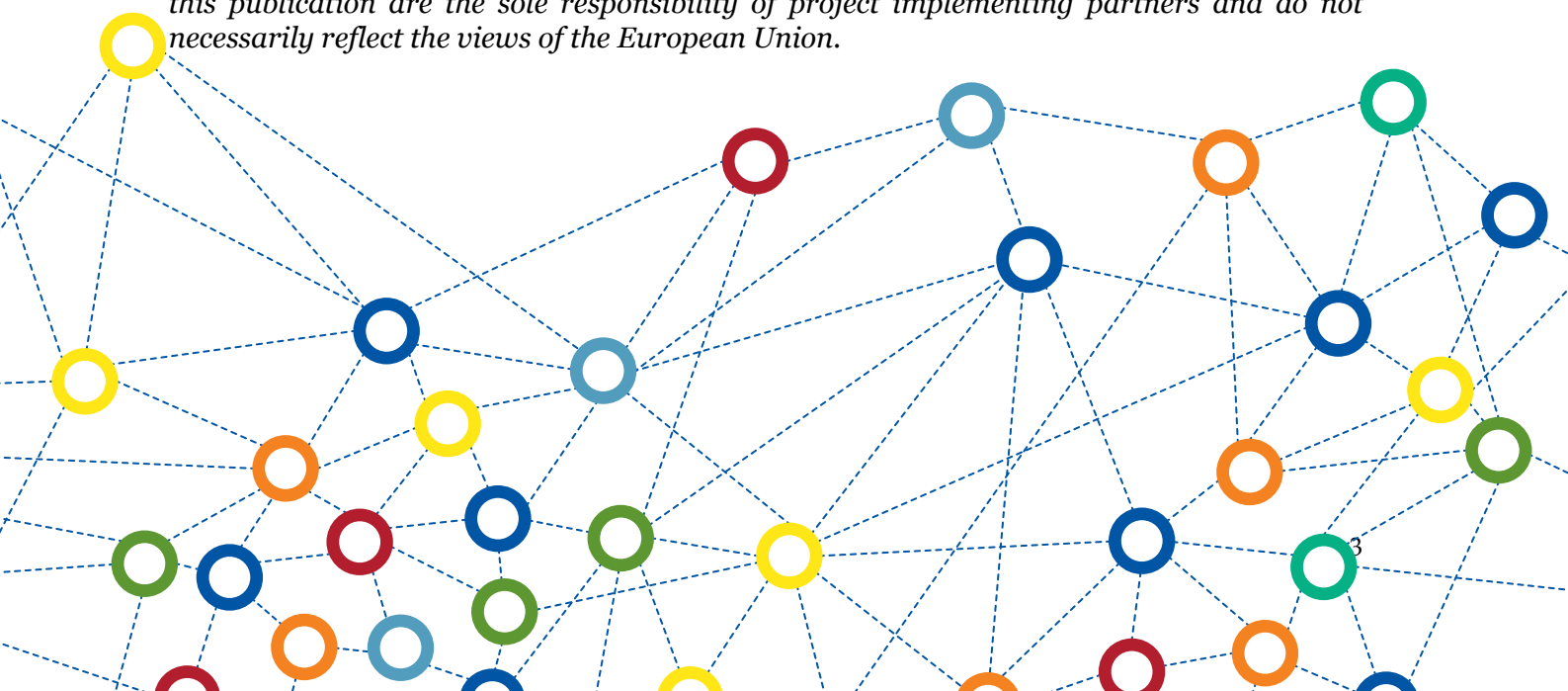
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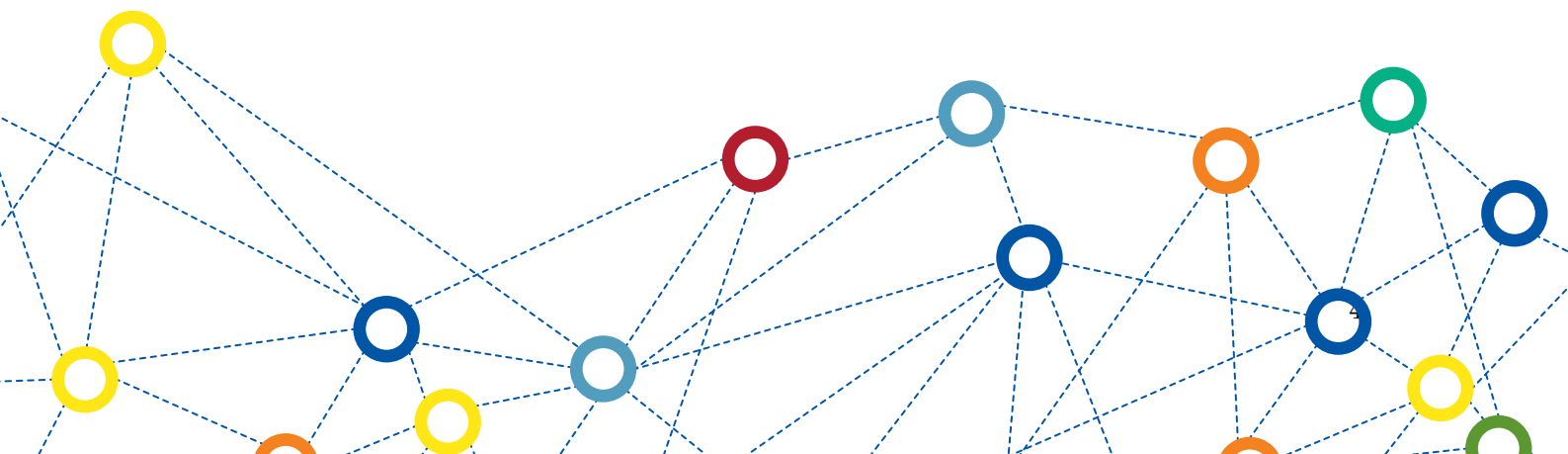
The recommendations are based on the workshop held in Kazakh (Azerbaijan) and series of pilot events held in partner countries with participation of entrepreneurs and local-government representatives.

The project partners and authors of these recommendations extend their hope that the information gathered in this report will help national and local governments and SME organisations supporting regional SMEs to flourish and therefore become the backbone for further growth of Eastern Partnership countries bringing them closer to the European Union.

However, it should be noted, that there is no panacea for SME growth in regions, no definite blueprint of the precise measures that each region should take. Each local authority has to define its own priorities for SMEs and implement its own measures, based on an analysis of the situation in the region.

Not all the actions proposed in these recommendations can be implemented in all regions. Some decisions should be taken at the national level. Nonetheless, these recommendations provide a variety of approaches for focusing regional economic policy on the needs of SMEs.

And finally, definitely - there are some solutions not included here. Be brave, implement them, share your experience, help others to become better!







# 1. THE ROLE OF SMES IN REGIONAL DEVELOPMENT AND WHY PROMOTING THEIR GROWTH IS BENEFICIAL TO ALL

Small and medium-sized enterprises (SME) in the European Union (EU) and also in EU Eastern Partnership countries are the main pillars of the economy. SMEs are very grounded in the regions in which they operate. They are part of the local society, a backbone of the local community.

SMEs are the main driving force for economic growth, innovation, a healthier regional economic development, employment and social integration in the regions. Thanks to their connections in their region, SMEs display a higher level of loyalty to their community and usually are involved in the regional development in multiple areas.

Thus, every region directly benefits from economically strong SMEs, not only by providing economic dynamism, more jobs, but also creating a positive environment that stimulates local development also thanks to role models of successful local entrepreneurs.

How to define what is an SME?

When speaking about SMEs, there are slightly different criteria used in each Eastern Partnership country to define what is considered an SME. For the purpose of these recommendations a definition accepted in the EU is used.

The main factors determining whether a company is an SME are:

1. number of employees,
2. turnover or balance sheet total.

Company category	Employees	Turnover	Balance sheet total
Micro	< 10	≤ EUR 2 m	≤ EUR 2 m
Small	< 50	≤ EUR 10 m	≤ EUR 10 m
Medium-sized	< 250	≤ EUR 50 m	≤ EUR 43 m

Therefore, maintaining a broad base of SMEs is crucial for the economic development, wealth and sustainability of a region. It is up to local and regional governments to pursue an SME and economic policy that is tailor-made to their specific strengths, to particular regional circumstances and to economic, technological and demographic processes in the region.

Although, attracting a large scale enterprises to the region could instantly provide more job opportunities for people or tax incomes for the municipality, the jobs available in these companies not always are corresponding to the skills of the local population and large investments in the region usually are associated with considerable tax cuts for the investor. Also, a large foreign investor not always is able to blend into local community and become a driving force for the overall growth of the region. Therefore, developing the region's internal potential like local SMEs, might be a more sustainable decision. Maintaining and developing existing companies in the region, promoting start-ups and, increasingly, business succession is becoming more important and must be the focus of regional activities in future.

Regional economic and SME policy nowadays is faced with new tasks. In the past a regional policy could concentrate mainly on providing suitable infrastructure (transportation, industrial and commercial premises), investment aid to enterprises and location marketing, now the following aspects are gaining more importance:

- creating a regional environment in which there are positive conditions for companies by means of synergies and added value in cooperation and regional governance processes that the individual actors alone cannot achieve;
- creating tailor-made infrastructure with centres for start-ups, innovation and technology;
- developing innovation-oriented funding instruments for research, operational R&D, knowledge and technology transfer and science parks;
- promoting the formation of networks and clusters;
- supporting business start-ups with targeted instruments for the start-up and growth phase as well as for individual industries;
- supporting lifelong learning and training in SMEs;
- developing systemic thinking and acting in regional innovation policy (promoting cooperation between actors from the worlds of business, politics and science, and other actors such as transfer institutions, networks and clusters).<sup>1</sup>

Following sections of these recommendations contain several examples and tools that could help implementing these aspects.

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<sup>1</sup> Regional implementation of the SBA, European Commission, 2014 <https://publications.europa.eu/en/publication-detail/-/publication/cfb47ae4-abcf-4a18-8058-177976f15647>

## 2. REGIONAL SME PROMOTION: FOUR STORIES, FOUR APPROACHES



## DEVELOPMENT OF REGIONAL SME SUPPORT STRATEGIES. A STORY FROM UKRAINE

Writing and adopting a development strategy provides an opportunity to analyse current state of business environment at the national or regional level, set the goals you need to achieve and to define tools and means for reaching them.

### **Remember!**

To make sure a plan is implemented – it is crucial to set specific action plan with deadlines, responsible parties, reporting periods as well as to define evaluation criteria to measure if the strategy has been successful.

### **National Strategy for SME Development 2020 - Ukraine**

The National Strategy for SME Development 2020<sup>2</sup> is the first Strategy for development of the small and medium enterprise sector in Ukraine and was adopted by the Cabinet of Ministers on 24th May 2017. The development of the Strategy took into consideration international best practice including EU Small Business Act (SBA) as a basis for its structure.

The document creates the framework of the national SME development policy in Ukraine and includes the Action Plan as a mechanism for its implementation. It also foresees creation of special tools for monitoring and evaluation, as well as coordination between all key levels and between key stakeholders. The Strategy consists of six strategic objectives:

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<sup>2</sup> <http://www.me.gov.ua/Documents/Download?id=7a48c253-8e8e-4c1d-ad66-bbcb261b54ba>



1. Creating a favourable environment for SME development;
2. Improving an access to finance for SME;
3. Simplifying Tax Administration for SME;
4. Promoting Entrepreneurial Culture and Developing Entrepreneurial Skills;
5. Promoting SME Export / Internationalisation;
6. Improving competitiveness and developing the innovation potential of SMEs.

Within each of the strategic objectives, the Strategy proposed various measures and instruments such as:

- Improving information provision including enhancement of the state statistics system;
- Streamlining bankruptcy procedure and promoting the "Second Chance";
- Intensifying use of promissory notes;
- Developing and promoting entrepreneurship culture;
- Encouraging employers to train their employees;
- Fostering development of social entrepreneurship;
- Launching target initiatives with regard to clusters and value chains.

The proposed measures have different scope and relate to both national and regional levels. All the various existing tools compose a complex mechanism for entrepreneurship support within the national scope.

The Action Plan<sup>3</sup> represents a practical framework for implementing the Strategy. The Action Plan describes how the measures proposed in the SME Strategy may be implemented and defines the necessary details for monitoring and implementation of the document.

The Action Plan is in the form of a table with following columns: measure, rationale, timeline, responsible body(ies) and indicators. It is expected that the Strategy will be implemented partly with funds allocated from the state budget by the authorities responsible for the measures defined in the Strategy, supplemented with support from international technical assistance projects and funds from other resources not prohibited by law.

Neither the Strategy nor the Action Plan have an explicit regional dimension and do not oblige regions/cities to implement specific measures. Both documents leave scope for oblasts/cities to define appropriate tools and to define the regional/local SME policies according to the local specificities, strategies, needs and priorities, which are in line with the decentralisation reform taking place in the country.

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<sup>3</sup> <http://www.me.gov.ua/Documents/Detail?lang=en-GB&isSpecial=True&id=e7c3c93a-cdf4-405a-ad29-46dead91bddf&title=ProcedureToImplementTheStrategyForSmeDevelopmentInUkraineUntil2020>

## Regional SME development plans

All 24 regions of Ukraine have active Regional Development Strategies for period until 2020, as well as Action Plans for their implementation. Most of the oblasts prioritize the development of SMEs and entrepreneurship skills in regional/local policies but historically these directions do not have adequate funding from local budgets, which means that it is essential to connect with alternative sources of financing for effective implementation.

Among the most frequent measures related to development of the SMEs in the Regional Development Strategies of above oblasts are:

- Development of business support infrastructure (Cherkasy, Chernihiv, Ivano-Frankivsk, Mykolaiv, Ternopil, Lviv and Poltava oblasts);
- SME competitiveness (Chernihiv, Ivano-Frankivsk, Kharkiv, Ternopil oblasts);
- Informational support / consultancy for SMEs (Cherkasy, Ternopil, Lviv oblasts);
- Access to finance, microcredits for SMEs (Ternopil, Sumy, Lviv, Mykolaiv oblasts);
- Development of SMEs/entrepreneurial skills in rural areas (Ivano-Frankivsk, Ternopil oblasts).

The crucial role of regions and cities in SME development is explained by the fact, that regional and city government are accessible to the business sector, can meet representatives of SMEs, information on the economic situation and problems in the region, a good understanding of the needs of SMEs, etc. Such issues as training for SME employees, business-consultancy, administration of business procedures, etc. are usually resolved at the regional/local level.

Usually development of SME policies at the regional level have to ensure a consistent long-term perspective, however the common approach for drafting regional/local SME policies in Ukraine is to develop a number of short-term programmes.

Since 2010, there have been several attempts to ensure the SME development at the regional level. Regional and local planning documents, which are devoted to SME development in regions of Ukraine could be divided in to two main groups:

- Regional long- and short-term documents, which contain SME development issues as a part. These are the Regional Development Strategies (According to the Law “On State Regional Policy”) and short-term programmes for economic and social development (Law of Ukraine “On State Forecasting and development of Programmes for economic and social development”).
- Regional planning documents fully devoted to SME issues. These are regional and local Programmes for SME development (Law of Ukraine “On National Programme for small and medium entrepreneurship development in Ukraine”).

## How to develop a regional SME development strategy?

During the development process of strategies and programmes, most of the state bodies in Ukraine follow the methodology proposed by State Regulatory Service. The Programme usually consists of an analytical overview of the SMEs in respect to their influence on economic development. In some oblasts this analysis is accompanied by a SWOT analysis. The other notable parts of the Programmes are tables in the form of Action Plans with following information: measure, rationale, responsible, timeline, expected cost and amount of funding.

Developing and implementing the regional SME development programme includes several stages:

- Comprehensive analysis of the current situation with development and support of SMEs in a region;
- Identification of priority areas of SME support in the region;
- Development of programme tasks and measures needed to accomplish the programme tasks;
- Monitoring the progress in implementing regional and local SME Development programmes and specific measures under these programmes.

## Content of a basic SME development strategy.

1. Analysis of SME sector in the region;
2. SWOT analysis;
3. Vision;
4. Opportunities and risks for implementation;
5. Strategic objectives, measures and rationales;
6. Mechanisms for implementation;
7. Monitoring and evaluation.



Most of the Programmes have two-year timeline. The SME issues in Kyiv are included into the Kyiv Programme for Development of Entrepreneurship, Industry and Market. Some of the regions, such as Poltava, Kharkiv and Chernihiv, have the Programmes with a timeline of 2016/2017 - 2020.

Among the measures typically funded from oblast budget are:

- Micro-credits and loan interest subsidies (Entrepreneurship funds);
- E-services for entrepreneurs;
- Trainings on entrepreneurship/ rural development;
- Participation in exhibitions, fairs and conferences;
- Development of promotional leaflets of the region.



Along the municipal budget, the measures in the SME Programmes often involve alternative sources of funding, such as:

- Trainings on M-test<sup>4</sup> and better regulations;
- Study tours and international events;
- Projects competitions/call for proposal;
- Development of web resources;
- Establishment of business support centres.

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<sup>4</sup> The M-Test is part of the regulatory impact analysis introduced in 2004 by the Law “On the Principles of State Regulatory Policy in the Field of Economic Activity”.



Any strategy without specific programmes and activities to support the implementation of measures set in the strategy is doomed to a failure. Support programmes and activities might come in large variety starting from nation-wide grant programmes, tax cuts for SMEs and start-ups, exhibitions, fairs, congresses to simple sit-down of different sides, facilitating meeting between SMEs.

### **Remember!**

Implementation of most of the support activities require human and financial resources. Before committing to any of the activities, make sure you have them not only for short term but also in long term.

## **The State policy for SME development support in Georgia**

Georgia is at the forefront of reform among the six Eastern Partnership countries at successful implementation of the Association Agreement. Over the last period Georgian authorities have implemented a set of activities helping SMEs to grow, to improve quality of investment and business environment.

In 2014, Government of Georgia adopted Regional Development Strategies<sup>5</sup> for 2014-2021 for the regions of Georgia and in 2016 SME Development Strategy 2016 - 2020<sup>6</sup>, including Action Plan stating objective to support the development and growth of economic role of SMEs. The SME Development Strategy is based on the main principles of Small Business Act (SBA) for Europe, covering areas like improving SMEs' operational environment, access to finance, enhancement of skills, facilitation of internationalization and innovation activities.

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<sup>5</sup> <http://www.mrdi.gov.ge/en/news/regional-development-strategies-2014-2021-regions-georgia>

<sup>6</sup> [http://www.economy.ge/uploads/files/2017/ek\\_\\_politika/eng\\_sme\\_development\\_strategy.pdf](http://www.economy.ge/uploads/files/2017/ek__politika/eng_sme_development_strategy.pdf)

One of the targets of SME Development Strategy was improving access to finance for SMEs. As a result, due to changes in the legal framework allowing the provision of grants to commercial entities, an increase in the financial support offered by state agencies and the implementation of a multitude of financial education initiatives has followed, a number of state programs were launched and new institutions were set up.

## Enterprise Georgia

The state agency is the first government institution in Georgia mandated to facilitate export and private sector development through a variety of financial and technical support mechanisms. The Agency helps SMEs expand and enhance operations, become more market oriented, and turn new ideas into profitable businesses by offering them financial and technical assistance tools.

The Enterprise Georgia Agency promotes regional small and medium-sized businesses through various types of support mechanisms, in particular:

- industrial Direction, which is aimed at developing business, creating new enterprises and promoting the expansion and re-equipment of the existing ones by simplifying access to finance and technical assistance;
- hospitality industry development component representing an initiative promoting the development of hospitality industry;
- micro and small business support component, which provides financial support (grant program) and consultations to micro and small entrepreneurs.



## Produce in Georgia

Enterprise Georgia Agency operates a state program “Produce in Georgia”. As of August 2019, 521 businesses have been supported within the framework of the programme with total investment value amounting to more than GEL 1,186 billion and more than 18 270 new jobs have been created. Project is implemented in all regions of Georgia.

The programme also has introduced slightly preferential treatment for women in the selection process for the Micro and Small Business Support programme under Produce in Georgia programme. As a result, up to 40% of the programme’s beneficiaries in 2016 - 2018 are women entrepreneurs.



## Georgia's Innovation and Technology Agency (GITA)

GITA is the main institution tasked with providing financial support for innovation in Georgia, three schemes have been developed to this purpose:

- the Micro Grants,
- the Start-up Georgia,
- the Matching Grants programmes.

The Micro Grants Programme, launched by GITA in 2016, offers up to GEL 5 000 (≈ EUR 1670) to support entrepreneurs with funds for developing prototypes within the GITA infrastructure, participating in fairs and innovation competitions. Since the inception of the programme, GITA grants distributed to more than 200 applicants.



The Start-up Georgia Programme has a total budget of GEL 35 million (≈ EUR 11,7 million), with GEL 11 million (≈ EUR 3,7 million) disbursed in 2016 for the first round of the project. This programme issues grants of up to GEL 100 000 (≈ EUR 33 000) to develop a business model and go-to-market strategies for their products.

GITA complements its financial support with training, coaching, mentoring and consulting services for all programme beneficiaries. A specialised training on developing innovative business skills has recently been created and is being delivered throughout the country. Trainings on coding, robotics, intellectual property, digital marketing and export-oriented ICT skills are also regularly carried out on the premises of various innovation centres in Georgia's regions, registering currently over 2000 beneficiaries.

## Georgian Chamber of Commerce and Industry (GCCCI)

Supporting entrepreneurs in regions is one of the Chamber's main directions. Local SMEs are able to receive detailed information about the requirements for accessing the EU market through services, that are provided by DCFTA<sup>7</sup> Information Centres, including providing regular trainings on the ground, raising awareness of local businesses, boosting their development and improving the quality of their products to match European standards.

Until now 6,000 SMEs in Georgia's regions have been consulted and trained on DCFTA related issues via DCFTA Information Centre services offered by the GCCCI. Therefore, local entrepreneurs are now better equipped to compete on domestic

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<sup>7</sup> Deep and Comprehensive Free Trade Area (DCFTA)

market and take advantage of the opportunities provided by the free trade area with the EU.

## **EU4Business**

There has been considerable support provided by the EU boosting economic potential of Georgia in recent years. EU funding for projects in Georgia is provided in the form of grants, contracts and increasingly budget support.

There are 19 ongoing projects with EUR 64,7 million EU contribution to the ongoing projects. These projects provide improved access to finance and new markets, specific DCFTA adaptation support, training, advisory and consultancy services for SMEs, including in rural areas, targeted support for women in business and the development of clusters in specific sectors, as well as support for BSOs and civil society in supporting the implementation of DCFTA objectives.

In 2017, the bilateral EU4Business portfolio in Georgia was enlarged with two significant projects:

- Georgia on European way: Creation of Effective Model for DCFTA, which aims at strengthening the capacities of Georgian CSOs and BSOs with overlapping functions of CSOs along the DCFTA implementation process and along the implementation of the SME strategy for Georgia; and
- SME Strategy Implementation and CSOs for Sustainable Economic Development - Strengthening the role of CSOs in DCFTA and SME Policy Implementation in Georgia.

The latter project is empowering civil society organisations, especially from the regions of Georgia, to effectively engage and participate in DCFTA/ SME policy formulation. Both of them are classified under access to knowledge and business skills, while they are also responding to the access to markets challenge experienced by the SMEs in the regions

Among results of the EUR4Business programme could be mentioned:

- 711 million euros (about 1,78 million GEL) issued to companies;
- 63 000 enterprises supported (loans, training, consultations);
- 2 450 new jobs created.

## The European Neighbourhood programme for Agriculture and Rural Development (ENPARD)

EU support to agriculture is about raising the income of Georgian farmers. With the help of ENPARD, 1,500 cooperatives are registered today in the country. They unite 15,000 farmers. More than 280 cooperatives took advantage of EU's direct financial and technical assistance, the total value of which amounted to 13 million GEL. As a result, income and profits of cooperatives increased by 27% and 30% respectively. In many cooperatives the job index was doubled.



### Access to finance

The largest programme currently running in Georgia is the European Bank's for Reconstruction and Development (EBRD) DCFTA Programme - EU4BusinessEBRD Credit Line, with 70% of the total programme budget going to Georgia, which accounts for EUR 13,6 million. The second largest programme is the DCFTA Initiative East-invest implemented by the European Investment bank (EIB) fully launched in 2017. About EUR 11,4 million of this programme's budget should be spent in Georgia. The share of access to finance programmes in the country portfolio is 76%.



### DCFTA Adaptation Programme (DAP)

In the area of improving knowledge base and business skills the DCFTA Adaptation Programme (DAP), focusing exclusively on Georgia, received the largest EU contribution of EUR 4,5 million. The DAP programme is part of the larger Advice to Small Businesses programme of EBRD, which has mostly supported improving knowledge base and business skills in the EU4Business portfolio by organising trainings of local consultants and support of SMEs with advisory services from local and international advisors.

### EBRD Program "Supporting Women in Business"

Within the framework of the EBRD Program "Supporting Women in Business" was launched opening EUR 43,4 million credit line for women in micro, small and medium businesses. The aim of the program is to create specific, sustainable financial products for SMEs managed by women, providing consultancy services and know-how access.



## EU support for SMEs – summing up

In recent years the EU has supported Georgia in developing its economic potential through international cooperation. The European Union provides over EUR 100 million for projects in Georgia annually, covering areas such as governance and education, water and energy, human rights and security, democratization and civil society, conflict resolution, economy, trade and public finance management; infrastructure, environment and rural development, education, health and social development.

EU provides also a wide range of support to SMEs in Georgia. As evaluated by the SMEs themselves, the EU support has been most successful in the following areas:

- providing access to finance to SMEs and related advisory services;
- supporting a more competitive and attractive environment for SMEs;
- strengthening institutional capacity and policy implementation related to regional SMEs.

While most of the programmes have a regional angle, experiences gained during implementation of these programmes highlight the need to consider social, economic and political context of various regions. Thus, bilateral projects tend to provide a more tailored approach to the need of specific regions.

Long-term programmes, especially under the access to finance priority and also under the DCFTA Facility, are very effective as the process of scaling up SMEs takes time, and this is especially valid for SMEs wanting to trade with the EU.

Access to finance programmes are prevailing in the portfolio. This reflects the needs of SMEs in the region. It has been stressed out that finances and advisory services should go hand in hand as experience shows that this combination is most successful.



Acknowledging that SMEs are equal partners when deciding measures for the development of SMEs in the regions, should be one of the first decisions to ensure effective strategies. Finding right partners who could provide considerable input, maintaining the network by finding the best and most effective communication channels & dialogue platforms is a must for any local administration.

### **Remember!**

Although you might be tempted to communicate with large SME organisations hoping that they cover most of the business development issues, you might run in to difficulties to obtain a real sense on current issues, as people representing larger organisations might be as far from everyday business as you are.

## **Local entrepreneur councils**

Many municipalities in Latvia see the added value in working closely with their entrepreneurs. To set up a framework for an effective communication they have established local Entrepreneur Councils as permanent dialogue structures.

The councils have broad range of topics and responsibilities, including consultations on the regional infrastructure development like road construction, power requirements for business development, also local tax incentives, labour force issues, discussing priorities for investment of EU structural funds etc.



These incentives have also served as catalyst for consolidation of regional entrepreneurs in form of establishment of new regional business associations.

## Initiative “Support Small Business!”

The aim of the initiative is to invite SME's to promote their goods and services, customers – to choose SME's products and services, and medium and large businesses to emphasize the importance of SME's as important supply chain partner and support for local communities.

**Mission:** mobilisation of resources to support SMEs.

**Vision:** More micro/small companies with more customers.

**Strategy:** Attracting new customers and partners for SMEs by joining of activities and resources, raise of awareness and education.

**Tactics:** „Small Business Day” as easy to access free resource for participants which provides effective communication, advertising, interaction with consumers, specific consumer groups and cooperation with other entrepreneurs.

**Philosophy:** less administrative burden, increase of productivity and shorten the way to consumer.



## Index „Most Investment-Friendly Municipality”

Main purpose of the initiative is sharing best practice among participating municipalities and sending right signals to businesses and households.

The index is developed within the initiative “Support Small Business” of the Business Union of Latvia and is supported by the municipalities of Latvia, the Ministry of Environmental Protection and Regional Development and data agency “Lursoft”.

The index consists of a quantitative or statistical section and qualitative or self-assessment by municipality according to the activities implemented promoting entrepreneurship in their territory.



The index shows that not always only the large municipalities are most capable of promoting entrepreneurship. To the contrary, the index proves that in the regions with a regional development centre and in the regions with a local development centre, a wide range of support measures for the promotion of entrepreneurship, tailored specifically to the particular situation of the municipality and to the needs of the entrepreneurs is being implemented.

Municipalities demonstrate that cooperation is also very important – at a local and regional level, by being involved in various activities with business-related institutions, in order to strengthen the competitiveness and popularity of municipality entrepreneurs.

### Civil servants shadowing entrepreneurs

The initiative Civil Servant Shadows Company was implemented in 2019 for the first time by Ministry of Economy of Latvia in partnership with business organisations. It allows civil servants to gain new experience and expand their horizons by stepping into the “shoes of an entrepreneur”, where they are able to see first-hand how their regulations impact businesses and evaluate where improvements can still be made. At the same time, this initiative help strengthening the “consult beforehand” principle and facilitates the dialogue between the state and businesses, thus lessening the administrative burden as well.



As part of the initiative, business representatives can submit their idea or achievement, as well as problems, and thus directly participating in the evaluation process and begin looking for solutions with the respective state administration employee. At the same time, the entrepreneur can consult with the civil servant, as well as obtain advice on how to solve various problems. Meanwhile, the business representative also has the opportunity to advise the civil servant how the state administration could improve its working process and regulations, thus directly participating in the creation of regulations.



In recent years, SMEs have become one of the main accelerators in economies around the world. SMEs support and promotion mechanisms have been widely used in recent years, due to their role in the development of a competitive economy, their positive impact on income distribution, poverty reduction and ability to rapidly react to changing market conditions. In this regard, a number of financial and non-financial incentive mechanisms are in place in the countries studied.

Extensive research demonstrates that the development of SMEs in regions of Azerbaijan is not at the desired level compared to Georgia, Ukraine and their share in economic growth and employment is much smaller than in other developed and emerging economies. In developed countries such as those of the European Union - 98-99% of all enterprises are SMEs. Although in Azerbaijan 83,3% of all enterprises are small, it does not mean that the contribution of small business in the regions is high enough and in general Azerbaijan is still lagging behind.

There are several constraints hindering SME development in regions of Azerbaijan. These impediments include:

- high level of centralisation of SMEs in the Absheron district around Baku;
- non-diversified access to finance;
- limited access to markets;
- legal constraints;
- lack of entrepreneurial skills.

Entrepreneurs suffer from a lack of professional skills, training to understand market requirements, which impedes their business's growth. Also access to finance is one of the most rigid problems in Azerbaijan for SMEs; generally, in their current situation, most banks are not willing to give loans to SMEs. They are perceived more as potential risks than profitable investments. At the same time, the weak development of other incentive mechanisms also prevents the successful functioning of SMEs in




the country. For instance, microfinance institutions, which are considered the main pillars of small entrepreneurship in Georgia, Ukraine, have not been properly developed in Azerbaijan, as well as there is a clear lack of wide-ranging venture capital, loan guarantee programs also common in world practice.

During recent years, several measures have been taken to mitigate obstacles facing SMEs. Some state programs have been implemented in the country by the Baku Business Training Centre (BBTC), National Fund for Entrepreneurship Support (NFES) of the Republic of Azerbaijan, Azerbaijan Investment Company (AIC) and Azerbaijan Export and Investment Promotion Foundation (AZPROMO). Another relevant initiative, the ABAD project, which was established in the ASAN service last year, is one of the most important steps taken for the development of SMEs in the country.

However, statistical data and an in-depth analysis of SMEs' role in the national economy does not show positive impact of these measures yet. For example, although several superfluous laws were abolished by the president, survey data among local entrepreneurs still show significant uncertainty about the implementation of laws by government representatives and structures. The DCFTA could modernise Azerbaijan's economy, with improvement of technologies and infrastructure, and with new regulations with international standards that would allow products to be exported not only to EU countries but also to the rest of the world.

The accession to the WTO is a prerequisite for applying for the status of associated country to the EU, and therefore accessing the DCFTA. Countries that have joined the DCFTA (Ukraine and Georgia) counted on enormous financial support from the EU in order to empower their intellectual capital, establish stronger rule of law, and change the structure of government and industries, development of regional SME's. The imposition of and harmonization of international standards could bring better quality and more efficient production not only to Azerbaijan but also Ukraine, Georgia in order to diversify the economy and give opportunity to new entrepreneurs and SMEs to start new businesses in regions and to export to the EU.

Given the above, it can be concluded that although support to SMEs in Azerbaijan especially in regions is less developed, certain steps are already being taken. These steps are mainly related to the simplification of business registration procedures and improvement of tax administration. However, based on statistical indicators, these steps are still not satisfactory. Therefore, further incentives that take advantage of studying experience of other countries, especially EU and DCFTA member countries, would be advisable.



### 3. **CONCLUSION & RECOMMENDATIONS**

Recommendations to be considered by governments and municipalities in Azerbaijan, Georgia and Ukraine to facilitate development of regional SMEs are listed in the following section.

#### **Recommendations for Azerbaijan**

1. The situation in Azerbaijan is vital and promising for the development of SMEs in the regions. There are many policies in place supporting the newly opened companies and establishing a new platform to decrease the economic dependence of one sector - oil and gas. Despite the incentives taken, the share of SMEs in overall export and import operations are remaining at 8% which is very low. The lack of institutional support in Azerbaijan is the main obstacle that should be carefully evaluated and actions in this field must be taken.
2. Speeding up signing process of DCFTA and AA agreements in order to promote liberalisation and decentralisation of the economic powers in the country by incorporating their rules. This step will be crucial to starting an application of association to the EU.
3. In comparison to previous years, the number of SMEs and private companies has been increasing. It has taken place with the direct contribution of the government's special policies. Many legal reforms and legislative acts have been applied in recent years, but still there are several steps to be taken, several laws to be implemented by the government to improve the SME situation in the country, encouraging individual entrepreneurs to invest in their entities.
4. There should be individual approach to each manufacturing sector, paying special attention to regional SMEs, e.g., providing lower interest rates for loans to regional SMEs, in order to support small- and medium-sized businesses in the regions.
5. To support agricultural sector in the regions a new export programme focusing on export of agricultural products, also implementation of major infrastructure

projects necessary for small business would increase the share of SME production in the overall export balance.

6. To help SMEs competing with foreign companies to access international markets, it is necessary to harmonize agricultural sector, industry, manufacturing, technologies and transport sector to international standards.

## Recommendations for Georgia

1. The State support to SMEs is not systematic and is not oriented on long-term results. Furthermore, actions to raise awareness of small and medium entrepreneurs about the DCFTA are not sufficient. It is especially important to strengthen the work in the regions, particularly among companies without significant innovation potential and from remote regions.
2. Despite the positive economic growth in regions, it has not had considerable impact on local population and has not had a significant impact on reducing unemployment and poverty rates. Local governments, who are responsible for creating favourable conditions to local population, should consider SME development as one of the priority areas, should design specific tools and make more significant efforts to support regional SMEs.
3. It is necessary to help existing and functioning businesses in rural areas in marketing, selling their products, therefore it would be helpful if, together with help for starting new businesses, the market outreach component could be strengthened and considered a priority.
4. Competition and market dominance of larger businesses slows development of SMEs in rural areas; therefore, it is necessary to pay special attention to creation of strong SME support institutions to help further development of regional SMEs and strengthen their competitiveness.
5. To stimulate SMEs in rural areas through support to agricultural sub-sectors that demonstrate strong potential creating jobs and increasing revenues of micro, small and medium enterprises (MSME).
6. To ensure sustainability and reduction of illegal migration, that has reached threatening heights and critically affects the demographic situation in Georgia, it is necessary for the regional governments to strengthen support and to facilitate entrepreneurial activity of women through a variety of financial and technical support mechanisms.
7. Georgian government should ensure compatibility of adopted strategies and legal acts with aims and spirit of Association agreement putting emphasis on the effective implementation of the provisions of the EUs Small Business Act and develop and set clear benchmarks for medium/long term regional SME development strategy, support and strengthen to business contacts and stimulate internationalisation of business activities in regions Georgia, in particular through expansion of their relations with European businesses
8. Access to finance is one of the major factors hindering regional SME development in Georgia. In addition, most of the entrepreneurs are not able to provide collaterals for the loans because they are set at as high as 120% of the

loans. Particularly acute is the issue of start-up micro and small businesses in regions, including women entrepreneurs, as the owners of real estate are mostly men.

9. It is highly desirable to encourage entrepreneurship with a credit guarantee system and a cheap credit state program, and to attract private investment and venture capital funds, which could significantly improve access of small and medium-sized entrepreneurs to credit resources. Innovative non-lending financing channels such as private equity, venture capital or crowd funding although being targeted by the SME initiative are still underdeveloped. It is necessary to implement legislative amendments to simplify financial accounting rules and procedures for small and medium businesses, and create more solid legislative support for its development

## Recommendations for Ukraine

1. To use the best EU practices, e.g. Initiative “Support Small Business!” or Index „Most Investment-Friendly Municipality”.
2. To provide activities aiming at supporting involvement of SMEs in EU programmes such as COSME and Horizon 2020. To conduct activities stimulating involvement of Ukrainian SMEs in COSME programme (practical workshop on EEN, preparation of leaflets on EEN, Erasmus). Considering that the only non-financial tool available in Ukraine is the COSME programme, it makes sense to pay more attention to Horizon 2020 since this EU tool provides access to alternative financial sources for SMEs. It is proposed to conduct an awareness raising campaign, organise a workshop for Ministry of Economy and a Roadshow for innovative SMEs in regions to facilitate SMEs participation in EU programmes (Horizon 2020, COSME, etc.)
3. To promote financial literacy among the public and build financial management and business planning skills among small business owners. To enhance financial skills of SMEs by training entrepreneurs on how to raise financing: cooperation with banks and investors, basics of finance, business planning, financial projections, etc. To train SMEs on how to acquire alternative financing such as leasing, factoring, credit unions, venture capital, business angel financing, etc.
4. To deliver basic free business services to SMEs within existing public sector institutional infrastructure through joint efforts of institutional and private players. SME Support Points should be the focal points specialised in providing business information, signposting, problem solving and also plug-in platform for interested partners to contribute into business development in a given locality or region. SME Support Points should be carried out in the growing number of the Centres for Administrative Service with the potential to scale up to comprehensive national coverage in the future. Integration of the information and advice components into the centres, where appropriate, will enable them to respond to the typical spectrum of basic needs of entrepreneurs such as: information about business establishment; taxation; labour regulations; access to finance; available support programmes; public procurement, etc.

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