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Business environment of SMEs in the Slovak Republic in the context of evaluation of international and domestic institutions

Abstract: Small and medium-sized enterprises play an important and irreplaceable role in the market economy. A key condition for their functioning and further development is a high-quality business environment. The study purpose is to evaluate the business environment in the Slovak Republic according to selected specialized international and domestic assessments. The most frequently used methods include qualitative and quantitative research, thanks to which a more comprehensive view of various areas and specifics of the business environment can be obtained. This article is based on selected quantitative surveys. Findings of the 2021 Global Entrepreneurship Monitor point to the need for further simplification of the conditions for starting a business, as more than half of Slovaks are convinced that it is not easy to start a business in Slovakia. According to the Business Environment Index, Slovak entrepreneurs perceive the worst situation in the area of price stability when evaluating the second half of 2022. Based on the results, we recommend some measures for improving of the business environment.

Keywords: business environment, small and medium-sized enterprises, Global Entrepreneurship Monitor, Business Environment Index.



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Podnikateľské prostredie MSP v SR v kontexte hodnotení medzinárodných a domácich inštitúcií

Abstrakt: Malé a stredné podniky zohrávajú dôležitú a nenahraditeľnú úlohu v trhovej ekonomike. Kľúčovou podmienkou pre ich fungovanie a ďalší rozvoj je vysokokvalitné podnikateľské prostredie. Cieľom článku je zhodnotiť podnikateľské prostredie v SR podľa vybraných medzinárodných a domácich hodnotení. Podľa zistení 2021 Global Entrepreneurship Monitor je potrebné naďalej zjednodušovať podmienky pre začatie podnikania, nakoľko viac ako polovica Slovákov si myslí, že založiť podnik v SR nie je ľahké. Podľa Indexu podnikateľského prostredia, podnikatelia v SR vnímajú za 2. polrok 2022 najhoršie situáciu v oblasti stability cien. Na základe výsledkov z týchto hodnotení navrhujeme opatrenia pre zlepšenie podnikateľského prostredia.

Keywords: podnikateľské prostredie, malé a stredné podniky, Global Entrepreneurship Monitor, Index podnikateľského prostredia.



Abbreviations:

SMEs – small and medium-sized enterprises

GEM – Global Entrepreneurship Monitor

BEI – business environment index

BAS – Business Alliance of Slovakia

SR – Slovak Republic

APS – adult population survey

NES – national expert's survey

Introduction

Small and medium-sized enterprises represent the most important segment in the business environment of almost every economically developed country. They are an important source of economic growth and bring innovative products to the market.

According to the BEM (*Business Environment Monitoring, 2023*), in 2022, SMEs accounted for 99.9% of the total number of business entities in the Slovak economy. They account for almost two-thirds of employment in the corporate economy and contribute by more than half to the total added value.

Positive benefits of business for society are primarily based on the creation of optimal conditions for its realization, as well as on the implementation of measures from regularly implemented measurements and analyzes of the needs and satisfaction of business entities. It is very important to monitor the quality of the business environment more intensively in times of uncertainty and changes brought to the market by the coronavirus pandemic. Creating suitable conditions for business is necessary at the current time, because the willingness to do business can be reduced in times of uncertainty. It is the task of the state, based on research, to systematically understand the pulse of the business environment, to create mechanisms for its continuous improvement, as well as to actively and effectively communicate them. Given the current situation on the market, it is also desirable to identify barriers that prevent or complicate the start-up of a business, or its development, promptly remove them and continue to simplify the entire mechanism of implementing business activities (*Správa o stave MSP 2022*).

For the purpose of better knowledge and understanding of the business environment, a number of different research approaches and methods are used. The most frequently used methods include qualitative and quantitative research, thanks to which a more comprehensive view of various areas and specifics of the business environment can be obtained. This article is based on selected quantitative surveys.

Specifically, it is the Global Entrepreneurship Monitor project (*Monitor GEM ..., 2023*), which brings together researchers from all over the world and publishes one of the world's most important studies about business dynamics. How the business environment is perceived by the

entrepreneurs themselves is revealed by the Business environment index elaborated the Business Alliance of Slovakia (*Index podnikateľského prostredia, 2023*).

Characteristics of SMEs in the Slovak Republic

In Slovakia, enterprise is taken from the broad point of view, in accordance with the Commission Recommendation 2003/361/EC of 6 May 2003 as „an enterprise is any entity engaged in an economic activity, irrespective of its legal form“ (*Commission Recommendation ..., 2003*). It is the economic activity that is the determining factor, not the legal form. In practice, this means that the self-employed, family firms, partnerships and associations or any other entity that is regularly engaged in an economic activity may be considered as enterprises.

In the article, we apply the size categories of enterprises resulting from the recommendation of the European Commission no. 2003/361/EC of May 6, 2003 on the definition of micro, small and medium enterprises and Commission Regulation (EU) no. 651/2014 of Annex I (*Regulation ..., 2023*).

Based on the above-mentioned documents, the following three criteria are considered when defining an SME:

- staff headcount,
- annual turnover,
- annual balance sheet amount.

The most important size criterion, which must always be met, is the criterion of employment or number of workers. However, the number of employee's criterion is supplemented by two other financial criteria, of which the company must meet at least one of them. When classifying a company as an SME, one of the following possible combinations of assessment is compared: (1) number of employees and annual turnover, or (2) number of employees and total annual balance sheet amount.

A change in the status of an enterprise as an SME, or a small enterprise or a micro-enterprise within the set of SMEs, occurs only after exceeding the size criteria in two consecutive accounting periods. Based on this definition, the group of small and medium-sized enterprises includes business entities that employ less than 250 people and whose annual turnover does not exceed 50 million Euros and/or the total annual balance sheet does not exceed 43 million Euros. Individual size categories of small and medium enterprises are determined according to the threshold values of the above criteria (*Table 1*) [1].

Basic quantitative indicators characterizing the state of the SME sector include their number. According to the data of the Statistical Office of the Slovak Republic, there was an increase in the number of small and medium-sized enterprises in 2022. The achieved growth was 5.7%. In absolute terms, the number of active SMEs was 670,161 (*Figure 1*). In a year-on-year comparison, the number of SMEs increased by 35,852 entities. From the point of view of the individual size categories of enterprises, the most dynamic increase in numbers occurred in the group of micro-enterprises with 0-9 employees, by 5.8% year-on-year. In the case of other size categories of SMEs, no significant changes were recorded.

The business sector in Slovakia has long been characterized by a high representation of micro-enterprises (*Atlas MSP na Slovensku, 2021*). Of the total number of active business entities in 2022, micro-enterprises accounted for up to 97.6%. Small (2.0%) and medium-sized

enterprises (0.4%) have a significantly lower representation. The sectoral structure of SMEs is characterized by the most significant representation of the service sector (*Figure 2*).

From the viewpoint of the structure of SMEs by ownership, privately owned SMEs clearly dominate (*Figure 3*).

In the structure of SMEs according to legal forms, natural persons – self-employed persons (60.3%) prevail despite the continuous decline in their representation. Even though the number of SMEs – legal persons increased year-on-year, their share in the total number of SMEs decreased to 39.7% in 2022.

The majority of SMEs in Slovakia develop their activities in the Bratislava region.

In 2021, small and medium-sized enterprises achieved a 74.3% share of employment in the corporate economy. The share of SMEs in total employment in the SR economy was 59.0%. Despite the support measures taken to maintain employment, the average number of employed persons in the category of small and medium-sized enterprises (including natural persons – self-employed persons) decreased year-on-year by 0.8% (by 10.9 thousand) to 1,390,000 employed persons. Employment in the SME sector declined for the second year in a row. Medium-sized enterprises had the biggest problem keeping their employees, whose employment decreased by 6.1% year-on-year. Microenterprises recorded a decrease in employment by 4.6%. The average number of persons employed by natural persons – self-employed persons has hardly changed.

Shortly, as we stated, there was an increase in the number of small and medium-sized enterprises in 2022. Of the total number of active business entities in 2022, micro-enterprises accounted for up to 97.6%. Despite the support measures taken to maintain employment, employment in the SME sector declined in 2021 for the second year in a row.

Business environment in the context of evaluation of international and domestic institutions

Global Entrepreneurship Monitor

Project brings together researchers from all over the world and is behind one of the world's most important studies on business dynamics. GEM sets three priority goals: to measure differences in the level of entrepreneurial activity between countries, to reveal the factors that influence the level of entrepreneurial activity in individual countries, and to propose policies that can increase the national level of entrepreneurial activity. The information is updated annually on two levels. The first is an adult population survey (APS) with a representative sample of at least 2,000 respondents. The second level consists of a survey of national experts (NES). Slovakia has been a part of the Global Business Monitor continuously since 2011. The results of the GEM survey of the adult population (APS) in 2021 point to a decrease in the perception of good business opportunities in their surroundings.

In a year-on-year comparison, the representation of respondents who perceive suitable business opportunities decreased (by 7.5 p.p.) to 33.4%. The relatively high self-confidence of Slovaks, which in recent years was manifested in a high perception of their knowledge and skills, which are necessary for starting a business, was not confirmed in 2021. Year-on-year, the perception of one's own knowledge and skills for starting a business in Slovakia decreased by 14.6 p.p. to 41.8%. Social attitudes towards business have been improving in Slovakia in recent years. More than half of the respondents (52.4%) consider entrepreneurship to be a suitable

career choice. In a year-on-year comparison, this represents an increase of 3.1 p.p. The perception of successful entrepreneurs and the associated social status has slightly worsened. More than half (55.6%) of Slovaks believe that success in business is associated with social recognition.

In 2020, almost two-thirds (62.1%) of the population thought that successful entrepreneurs are recognized. In Slovakia, the fear of failure would deter 46.0% of the population who see business opportunities, which represents a slight decrease compared to 2020 (48.7%). The majority of people in Slovakia (54%) personally know at least one person who started a business within the last 2 years, while every fourth resident knows more than one entrepreneur. The results of the survey further point to the need for further simplification of the conditions for starting a business, as more than half (60.5%) of Slovaks are convinced that it is not easy to start a business in Slovakia (*Figure 4*).

Thus, the representation of respondents who perceive suitable business opportunities decreased according to GEM. The relatively high self-confidence of Slovaks, which in recent years was manifested in a high perception of their knowledge and skills, which are necessary for starting a business, was not confirmed in 2021. Year-on-year, the perception of one's own knowledge and skills for starting a business in Slovakia decreased.

Business Environment Index

Since 2001, Business Alliance of Slovakia has been recording the development of entrepreneurs' opinions on the state of the business environment in the Slovak Republic through Business environment index, which makes this index unique in the Slovak Republic. At the same time, entrepreneurs regularly comment on the laws adopted in the given period and evaluate their importance and their benefit for the business situation.

BEI is a feeling index that captures the perception of entrepreneurs on the development of selected parameters of the business environment. It does not indicate the absolute quality of the business environment, but reflects the perception of entrepreneurs. They indicate the shift in 15 areas with the values +3 extreme improvement, +2 significant improvement, +1 moderate improvement, 0 no change, -1 moderate deterioration, -2 significant deterioration, -3 extreme deterioration. Negative values of the index may not mean that the business environment is necessarily deteriorating, but they may testify to the prevailing pessimism of entrepreneurs.

Currently, BAS publishes the 74th value of the IPP index, which captures its changes for the second half of 2022 (*Table 2*). This represents a horizon of 21 years. 65 business entities participated in the IPP survey for the second half of 2022.

Almost 94% of the interviewed businessmen evaluate negatively the situation in the area of price stability (inflation and stagflation) in the second half of 2022.

Inflation affects the business in many ways and its impact is reflected in the overall operation and life of the business. It has the most significant effect on changes in the prices of inputs and outputs, while these changes are generally uneven. The higher the inflation rate, the more intense and faster the changes (*Ekonomický a menový vývoj, 2022*).

The business sector is exposed to more significant effects of inflation than households. Businesses face a faster increase in input prices than households. The prices of several commodities and goods grew dynamically during the entire year 2022, while this price growth

spills over into an increasingly wide range of goods. The most significant year-on-year price growth is present in energy commodities (*Indexy cien ..., 2022*).

As Figure 5 shows, the prices of industrial producers for the domestic market were 38.1% higher year-on-year in November 2022. This was a significant slowdown in the dynamics of producer price growth, as the previous three months the producer price growth exceeded the level of 50%. The prices of materials consumed in the construction industry continued to reduce the growth rate and reached below 15%. Agricultural products were 39% more expensive year-on-year.

In this regard, The Ministry of Economy of the Slovak Republic provided subsidies to companies to cover additional costs due to the increase in gas and electricity prices as early as December 2022, and plans to continue this this year as well (*Dotácie na energje, 2023*).

According to the survey, the second area in which the situation has shifted for the worse in the second six months of 2022 is political culture and the functionality of the political system (85%).

According to almost 78% of the interviewed entrepreneurs, the third biggest worsening of the situation occurred in the sustainability of public finances and the efficiency of state management.

Entrepreneurs perceive the most significant improvement in the situation in the first half of this year in the area of performance, productivity and profitability (29%).

Thus, of the interviewed businessmen themselves evaluate negatively the situation in the area of price stability (inflation and stagflation) in the second half of 2022. Regarding this, businesses face a faster increase in input prices than households. Other areas negatively evaluated are: political culture and the functionality of the political system sustainability of public finances and the efficiency of state management.

Conclusion

Due to the economic and social importance of SMEs for the Slovak economy, it is necessary to monitor and improve the business environment for their development.

The results of the GEM survey in 2021 show that the relatively high self-confidence of the adult population in business in Slovakia, which was manifested mainly in the perception of their knowledge and skills, which are necessary for starting a business, has decreased. Self-confidence of Slovaks in business is hampered by fears of possible failure. Year-on-year, the perception of one's own knowledge and skills for starting a business in Slovakia decreased by 14.6 p.p. to 41.8%. 40.9% of Slovaks perceive good business opportunities in their surroundings. Compared to 2020, their share decreased by 7.5 percentage points. The perception of successful entrepreneurs and the associated social status also slightly deteriorated. The majority of Slovaks (60.5%) are convinced that it is not easy to start a business in Slovakia.

According to Business Environment Index, which is a feeling index capturing the perception of entrepreneurs on the development of selected parameters of the business environment, almost 94% of entrepreneurs assesses negatively the situation in the area of price stability (inflation and stagflation) for the second half of 2022.

Support for the establishment and growth of businesses, especially small and medium-sized enterprises, is one of the key activities that ultimately increases the performance of not only

regions, but also the entire economy. In accordance with the needs of SMEs, it is therefore still necessary to continue to improve the efficiency of support for SMEs (at the regional and national level). Business support is an important tool for the development and stabilization of the business sector and the country's competitiveness. To support a stable business environment, it is necessary to continuously continue in the systematic cooperation and coordinated approach of all involved departments, as well as to take into account the proposals and recommendations of individual entities. Mutual and intensive cooperation should aim at improving the business conditions of SMEs.



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Notes:

- [1] These ceilings apply to the figures for individual firms only. A firm that is part of a larger group may need to include staff headcount/turnover/balance sheet data from that group too.



Appendix

Table 1. Definition of SMEs

| Company category | Staff headcount | Turnover | And/or | Balane sheet total |
|------------------|-----------------|----------|--------|--------------------|
| Medium-sized | <250 | ≤€50m | | ≤€43m |
| Small | <50 | ≤€10m | | ≤€10m |
| Micro | <10 | ≤€2m | | ≤€2m |

Source: Author according to EU recommendation 2003/361

Table 2. BEI value. Second half of 2022 (in %)

| Aspect | Deterioration | Improvement |
|----------------------------------|---------------|-------------|
| Price stability | 94 | 3 |
| Political culture | 85 | 5 |
| Sustainability of public finance | 78 | 6 |
| Law measures | 69 | 5 |
| Stability and quality of inputs | 57 | 12 |
| Access to financial sources | 53 | 3 |
| Labour-law legislation | 52 | 14 |
| Bureaucracy | 52 | 8 |
| Workforce | 51 | 5 |
| Tax-levy legislation | 42 | 11 |
| Enforceability of law | 38 | 5 |
| Trade partners | 38 | 9 |
| Productivity of business | 38 | 29 |
| State institutions | 20 | 20 |
| Corruption | 17 | 18 |

Source: BAS

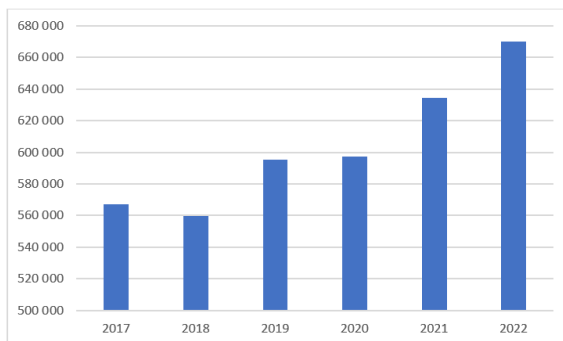


Figure 1. Development of the number of SMEs (Author, according to data of the Statistical office of the SR)

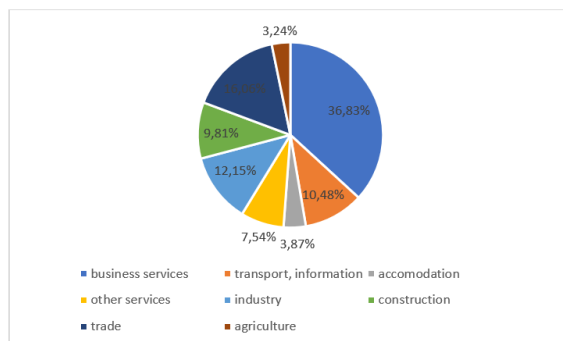


Figure 2. Sectoral structure of SMEs – legal persons in 2022. (Author, according to data of the Statistical office of the SR)

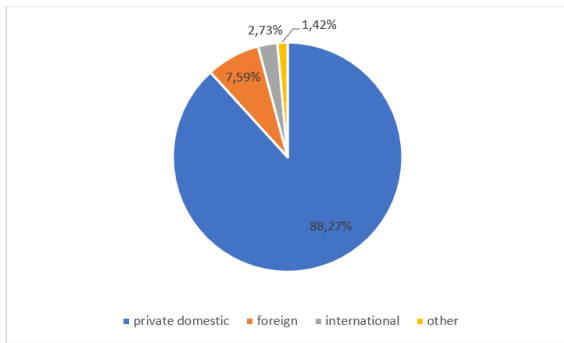


Figure 3. Structure of SMEs according to the ownership
(Author, according to data of the Statistical office of the SR)

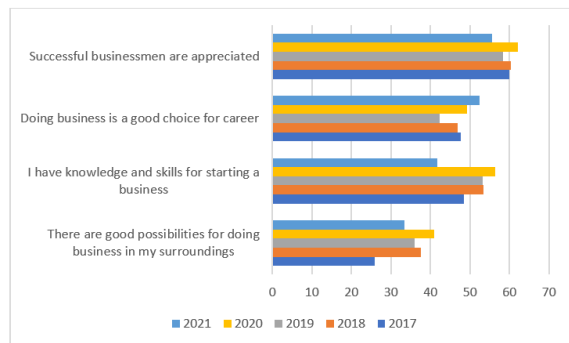


Figure 4. Selected approaches of the Slovaks to entrepreneurship (in %)
(Author, according to data of GEM)

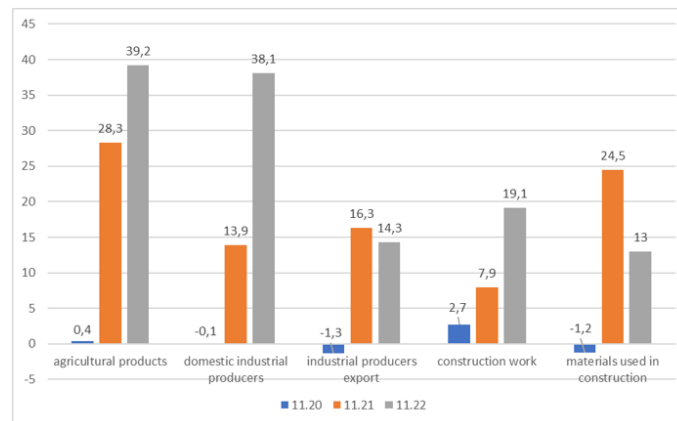


Figure 5. Price change in the production sector (year-on-year in %)
(Author, according to the Statistical Office of the SR)