

INTERNATIONAL BUSINESS PROSPECTS OF SMALL AND MEDIUM ENTERPRISES IN SERBIA

Bojan Zdravković, Fakultet za poslovne studije i pravo,
ALFA Univerzitet, Beograd,

Abstract: *The subject of this document is an analysis of factors affecting the export business of small and medium enterprises (SMEs) of the Republic of Serbia. Through reference indicators, the author tries to prove hypothesis that the extent and pace of internationalization of SMEs in Serbia is directly related to the generally poor state of economy in Serbia. The author also points out the similarities and differences in the process of internationalization of small and large enterprises in transition countries of Central and Eastern Europe (CEE) with special emphasis on the relationship between large and small companies in Serbia and the impact of that relationship to their external business.*

Keywords: *SMEs, internationalization*

SERBIA - ECONOMIC INDICATORS

Economic environment of the Republic of Serbia cannot be positively evaluated! According to the statistics of the World Economic Forum (1) Serbia is far behind the least developed countries of the European Union. In recent years, the position of Serbia on the list of Global Competitiveness Index gradually falls. In fact, according to 2010 data, the ranking order with 139 positions (states), Serbia is in the 96th place, three points ranked lower than in 2009, and even 11 points compared to 2008. Of the countries in the region, the worse position record Bosnia and Herzegovina, in 102nd place. In front are, Macedonia (79), Croatia (77), Albania (88), while the best placed is Montenegro (49).

According to market efficiency, Serbia is the last among the 139 countries that are subject to assessment. The cause of this poor workflow is the number of dominant players in the market. By the strength of competition, Serbia is in the 131st place, while only two countries have more ineffective anti-trust policy than Serbia has.

Serbia is characterized by low levels of innovation activities in comparison with the EU and new Member States. According to the report of the World Economic Forum in 2007, Serbia was on the 79th place among 104 countries. In the meantime, the situation is slightly improved.

According to the Labour Force Survey (LFS) (2) of the Statistical Office conducted in April 2010, sample of about 7,000 households, and in Belgrade, central Serbia and Vojvodina, the results are as follows: The unemployment rate in Serbia in April 2010 was 19.2 percent, and it has been expressed by gender: 18.6 percent for the male population and 20.1 percent for women. Observed by regions, the unemployment rate in central Serbia was 20.6 percent, 20.9 percent in Vojvodina, and in the city of Belgrade was 14 percent.

In order to complete the generally bad image of the Serbian economy, it is important to note that Serbia's public debt (3) at the end of September 2010 rose to 38.5 percent of gross domestic product (GDP), amounting to 11.62 billion euros. At the end of last year,

debt was 9.85 billion euros, which means that in the first nine months of this year debt increased by some 1.77 billion euros.

These parameters were not encouraging, especially if one takes into account the high level of external deficit in the global economic crisis.

THE STATE OF SME SECTOR IN SERBIA

Survey conducted by the Regional Development Agency in 2009, on a sample of 3,000 SMEs, showed that the biggest problems for SMEs were: (4) lack of funding and legislation, then the lack of suitably qualified workers, non-compliance of operations with the requirements of quality and lack of information on markets and technologies. The greatest dissatisfaction was expressed regarding tax regulations, procedures, and lengthy and expensive procedures for issuing building permits. After that, following the work of inspection bodies, problems with registration of real estate, complicated procedures for registration and deregistration of workers, slow collection of receivables. In the strategy of competitive and innovative SMEs in the period 2008 - 2013, which is an official act of the Government of the Republic of Serbia enacted to promote the SME sector, is provided the fact that one of the biggest problem of Serbia is slow and expensive administration. For establishing a company in Serbia in 2008, 11 different procedures, 23 days and 8.9% of gross domestic product per capita (10.2% in 2006) were necessary. The procedure is more complicated to obtain various types of permits (for construction, electricity connection, telephone, inspections or approvals from other agencies, to start a business, etc.). According to Strategy data, in circulation were about 20 procedures that meet the required time of 204 days and the obligation to pay 27 times higher values than the gross domestic product per capita.

The problems of abundance and conflicts of regulations and corresponding rules will be resolved during the implementation of the strategy of regulatory reform. First steps in that direction were made. While registration with the Agency for Business Registers (APR) people simultaneously obtain a VAT number so the time for starting the activity is shorter. From this year the annual accounts trainers are only in one place – at the APR, not in three places as before. Enforcement of the Law on Spatial Planning will put real estate in order.

The share of public sector in financing SMEs is significantly increased, especially in the field of microcredits for new businesses. More favorable credit terms than the market ones are provided, such as the cost of credit, terms of use, and the necessary guarantees.

The tax system in Serbia is very complex. It terms of time, for calculation and payment of taxes and other mandatory benefits companies spend even 279 hours while the number of annual payments is 66! If we take into account that the Swedes are taxed only twice a year, you can see the gap between Serbia and the more developed part of Europe. Lowering of tax rates is encouraging, so that the annual rate of income tax and VAT rates among the lowest in the region.

Rapid growth of the SME sector follows poor state of human resources, i.e. slow qualifying of entrepreneurs for new challenges. The positive aspect is the educational programs at the regional agencies, the Centers for SME development support, the National Employment Service, Chambers of commerce and specialized non-formal educational institutions. In many high schools, with the support of donors, the projects of Student Entrepreneurship are implementing. What stands out as a problem that needs to be eliminated is the inequality of implemented educational programs.

Attention of analysts and the entire system to support the development of these enterprises primarily is focused on the creation of these companies and their operations within the borders of the state while the less attention is paid to firms with cross-border ambitions. However, the key point in the dynamics of economic development is the small and medium enterprises working on getting on the foreign markets and internationalization of their production.

INTERNATIONALISATION OF SMALL AND MEDIUM ENTERPRISES

A successful operation in modern conditions is unthinkable without the involvement of the international trade processes. End of the last and the beginning of this century was marked by a significant increase in participation of SMEs in the European market and then began talk about their Europeanization. It is about the rise of exports and the dynamics of strategic partnerships with these companies in other countries. The four forms of internationalization of SMEs through the development of its international activities should receive were identified: (Okulić, M: page 122) (5)

- 1) Export,
- 2) Cooperation with foreign partners,
- 3) Licensing by foreign partners,
- 4) Investing abroad and selling technology to the world.

1. Dogma that small and medium-sized enterprises that export risks to achieve lower profits than those that produce for the domestic market is abandoned. However, research (Major, I: pp.1371-1396) (6) have shown that the majority of SMEs in transition countries of Central and Eastern Europe are not sufficiently flexible to adapt volatile market conditions faced by the countries to which exported. The most common problems are bureaucracy, weak institutional systems, and particularly uncertain property rights.

2. The second form of internationalization involves entering into strategic partnerships. Small and medium enterprises realize the integration of the function of the internationalization of business based on different forms of alliances based on common interest, such as an agreement on joint investment, association for achieving innovation, joint appearance on the market, cross-licensing, merger based on franchising, etc. The creation of export groups of small and medium-sized companies can be the first step towards creating a kind of cluster companies in which there is a critical concentration of certain competencies to compete successfully in a certain business, not only at national but also at global level.

Clusters are an extremely important way of organized appearing of small enterprises in Serbia. Ministry of Economy and Regional Development of Serbia supported the development of these cooperatives through the "Cluster development program in Serbia. This refers to changing legal environment and the provision of non-financial and identified as a priority.

Currently twenty-five clusters grouped according to stages of development is from zero to three is active. Clusters of zero phase are those who have just emerged or are in the initial years of operation, while the clusters of the third phase are in the advanced stages of development. The most successful clusters in Serbia are software cluster with 15, Automotive with 27 members, and cluster of the manufacturers of small agricultural machinery, which comprises 15 companies and 5 additional institutions. It is interesting that the rise of cluster producers of flowers in Šumadija is rising. (7).

However, according to the experts of the European Union and the Ministry of Economy, existing clusters are still poorly organized and management poorly trained. Their survival depends largely on public assistance. Compared with those in the European Union, our clusters are quite weak and would not be able to compete with European ones. According to the Ministry of Economy and Regional Development, the countries in the region have more clusters than Serbia. In Croatia, 44 is registered, 48 in Hungary, and in Bulgaria 50 clusters. Interestingly, however, in Slovenia there are only 10 regional clusters, while in Italy 213.

Despite the current unsatisfactory situation, attitude of the ruling elite is that the state should be able to create a favorable environment for the association of the companies and not to create clusters.

Franchising (Radosavljević, Ž: pp. 128-129) (8) is a special form of business cooperation between independent business subjects connected based on the agreement in which the franchisor gives users the right to use its trademark, image, and systems of work, and in turn charges a fee as a franchise. In Serbia, the most common form of product distribution is franchise. The highest percentage of small and medium enterprises is engaged in this field, where more than half of employees in Serbia work. On the other side, other transitional countries have had better luck in developing the concept of cooperation. Franchising is best developed in Hungary, which has 400 franchise chains, of which 50% were domestic. Followed by Poland and Slovenia with 120 franchises, of which 55.7% were domestic. In Croatia, operates 120 franchises donors, of which 30% were domestic. Czech has 55 franchises.

Experts point to the need for content-designed concept of franchising development in Serbia. As the main pre-conditions state: (Čuzović, S: page 228) (9)

- Socio-economic assumptions (stability of the political and economic environment, corporate culture),
- Development of entrepreneurial spirit among Serbian businesspersons,
- The necessity of strengthening of fair competition, transparency, lawful business, and the release of political influences,
- Raising the quality of products offered by Serbian businessmen,
- Long-term creation of brand names and not creating brands from season to season (e.g. duvan čvarci (a type of pork crackling), slivovitz) etc.

It is particularly important to reduce risk in business because franchising has traditionally had a lower failure rate to just stated jobs. When purchasing any of the franchise business concepts, many difficulties have been overcome and resolved. This helps ensure stability and growth of small and medium enterprises, which are extremely important for economic development, fight against unemployment, and ensure country's exports.

Serbian government has recognized the efforts of experts and through the Ministry of Economy and Regional Development is taking steps in the realization of this concept. For example, taking over Zastava Kragujevac by the "Fiat" may result in a greater number of business cooperation based on the model of franchising.

3. There is little data on the licensing of foreign partners or obtaining licenses from them. A survey taken a few years ago on the territory of the European Union showed that among 240 industrial SMEs only 6% provided licenses abroad!

4. Direct investments of small and medium-sized companies challenge the opinion that the direct investment abroad is the privilege only of large enterprises. Compared to the investments of big companies, direct investment of small and medium enterprises are much more harmonious with the development objectives of host countries. In addition, these enterprises in the form of foreign direct investments often cooperate with the local environment. Surveys conducted in the SME sector shows that foreign direct investments value the training of local staff as an important factor for its strategic success three times more. Then, it is more important to them to promote production and services and finally up to 50% is the training of local managers and increasing revenues in foreign markets important to them. (5)

Each national economy should create a strategy of inclusion in global trade flows. Toward defining the strategy, an important place should be allocated to the SME sector.

SME vs. MNCs - ADVANTAGES AND DIFFERENCES IN THE PROCESS OF INTERNATIONALISATION

SME sector has proven to be very "powerful industry" and its popularity continues to grow. SMEs contribute to employment growth much more than large firms and may in the long term to provide a very important share of all employees. In addition, SMEs can help in restructuring by absorbing redundant workers and increase competition on the market. However, the establishment of SMEs does not necessarily lead to the creation of profitable enterprise because the company primarily involves the willingness to take risks, and it is necessary to have both experience and keen sense for business.

A study (Svetličić, M Jaklič, A Burger, A: pp. 36-65) (10), conducted in five Central European countries in the sample of 180 companies (26 in the Czech Republic, 69 in Estonia, 22 in Hungary, 24 in Poland and 39 in Slovenia) indicates that the internationalization of the SME sector and large companies have many more similarities than differences. The subject of the study was the motives for going to foreign markets, possible barriers, and competitive advantages of the compared categories. Given the fact we are talking about members of European Union, the assumption is that because of time distance in relation to the period of investigation (2007) and the general backlog of our country in transition for these countries, the results may be identified with the current internationalization phase of Serbian small and large businesses!

Both groups of firms identified the same obstacles, but it turned out that SMEs face greater financial problems and problems of production capacity. Their colleagues enjoy greater superiority in the field of marketing and production capacity but lack of agility for a fast and efficient entry into the market too. As SMEs are often the target of specialized niches, the main competitive advantages of SMEs are technological know-how, organizational flexibility, and closer relationships with their customers. Larger players are relying on marketing and the benefits arising from economies of scale. Large companies dominate the production; small and medium-sized enterprises dominate in services of various kinds, such as hospitality, real estate, renting, and business activities, trade and construction. These branches are limited locally and cannot easily cross the borders. A similar study (Major, I. 2008) (6) showed that the number of SMEs in CEE in retail trade, personal services, and craft activities was two or three times bigger than the number of small enterprises in agriculture and food industry, particularly in relation on production, heavy chemical industry or mining.

Analysts have identified three motives for investing abroad: (10)

- 1) Search for new markets,
- 2) Hiring cheaper labor and reduction of other costs,
- 3) Search for strategic resources.

Investment motives of large companies are more diverse than those available to small and medium enterprises! Finding new markets is the most important motive for internationalization. Market motives are the market size, expected growth, purchasing power, and other aspects that may bolster sales abroad. Advantages associated with these motives are less expensive inputs, lower transportation costs, customs duties, taxes, and other benefits of the importing country and directly decrease the costs of the firm.

Both groups of companies estimate the market growth and purchasing power in deciding whether and where to invest. Lower labor costs and production costs are more important motive for investing abroad for larger companies. This is a significant difference between small and medium enterprises. Large firms are more sensitive to labor costs and have the ability to choose a location for foreign direct investments more carefully than the small and medium enterprises.

Global companies often manipulate the total profit achieved by using transfer pricing. Along with this goes the importance of price competitiveness. SMEs have an opportunity to exercise a competitive market position through transfer pricing. SMEs rely more on specialization, adaptation, and close relationships. Because of its specialization, small and medium enterprises are targeted to meet the needs of their clients and not just to sell products. This is especially true for highly specialized service companies, such as consultancy or intermediary in the sale between companies. Because SMEs usually focuses on specific niches, it is directed at meeting the needs of known customers and is often less flexible in terms of price.

Strategic resources include intangible assets such as patents, trademarks, and copyrights and other intellectual property rights, technology, know-how, access to technology networks and alliances. Large companies are more careful than small and medium when deciding where to invest and trying to acquire strategic assets. Frequent changes and problems with the application of the law that is a characteristic of transition economies

make business expensive. The main problems are *unstable and non-transparent legal environment* and turbulent administrative procedures in the countries of investments. However, SMEs are strongly encouraged to internationalize operations, when the legal systems in the target countries are not transparent and when the protection of property rights as is the case in many transition economies that are lagging behind in privatization and market reforms. (10)

SMEs have fewer employees and involve fewer problems in management. Lack of small business is that its management is still closer to actual practice and may lose a broader perspective. Another problem is the large share of family businesses among them. Family businesses often do not have the ambition and determination to expand their business abroad. Smaller organizations are directed to the supply of larger organizations with services and products, using its size and power to stifle the cash flow of smaller organizations. Successful small organizations inevitably become a large organization.

RELATION OF SMALL AND LARGE COMPANIES IN SERBIA

The current ratio of large and small companies in Serbia is characterized by discriminatory behavior of large companies. Mentioned discrimination refers to failure to settle the obligations of large to small and unequal position of small tenders for public procurement. In addition, it should be noted underdevelopment of distributive chains in Serbia.

Experts (11) points out that small and medium enterprise in Serbia are at the bottom of the priorities in the collection of their receivables from large ones. According to the applicable customs regulations, in that month in which the company meet its obligations to the Customs and VAT recovery can be performed i.e. offset VAT. Large companies should be allowed offset VAT only when settle their obligations to small and medium enterprises, and only to the extent to which they fulfill their obligation towards smaller firms. If in this regard the government has taken the same attitude as towards the settlement of customs duties, the budget would be smoother and more efficiently filled, and most small and medium enterprises would not have a liquidity problem. Large companies usually have a competitive advantage in terms of meeting the requirements and regulations of the *tender procurement system*, but many governments have taken measures to ensure equal status of the SME sector through better information and simpler tender procedures. Law on Public Procurement must stimulate the participation of SMEs in public procurement, and eliminate all restrictions that prevent small to get this jobs too referring to the amount of funds to participate in the tender, the size of the company, the amount of capital, and assets in the account, the number of employees and the like. The opinion was also that creation of a consortium of small and medium enterprises to participate in public procurement must be allowed. What kind of potential we are talking about is illustrated by the fact that Serbia spends around three billion euros in public procurement each year!

Developing of supply chains is an important prerequisite to acquire credibility, increase market competitiveness, and promoting technological development of small and medium enterprises in Serbia. In this way, Serbian companies have the ability to supply directly major regional and international companies. In this area, particular importance has introduction of customer relationship management (CRM system). In order SMEs to fight for the place in supplying a large company, quality certificate that shows that companies doing business in specific, recognizable standards are very important. The

more important is to meet the standards, but the occasional checks performed by auditors. (12)

Development of supply chains should be aligned with other economic measures, especially with good relations and cooperation between regional SME agencies and other organizations that provide support services to the SME sector, in order to integrate their activities at the local and regional level. Regional SMEs agencies should specialize in a new area of providing support to development of SMEs supply chains and to integrate it into their service of delivering support to SMEs operations. (Grozđanić, R, Savić, B: page 81) (13) The Serbian economy require institutions or agency that will connect domestic with foreign companies that will be able to provide information about where and what to buy and with whom they can work together to foreign companies, and that investors know where such information can be obtained. In addition, it is necessary to identify all companies that have the ability to collaborate with others. This is a very slow process because it takes time to make such database.

RESUME

An international business prospect of SMEs of Serbia is directly caused by the economic situation in our country. Serbian companies, often, face problems such as lack of funds to finance export activities, lack of trained and highly skilled labor, lack of knowledge of foreign markets, and the lack of information. Because of the backlog of privatization, the problem is lack of reliable local partners interested in external appearance.

In order to respond most effectively to these demands, companies need their strength to recognize the interconnection thus obtaining a strategic position in future operations as a group of companies. Connecting small and medium enterprises for export should be based on a thorough analysis of problems and opportunities that arise in the international market. Therefore, encouraging these companies to create a kind of export groups to address the aforementioned problems can be very important for success in implementing the strategy of entering foreign markets.

In terms of relationships with large companies, Serbia has no appropriate legislation that would force the big companies in a different relationship to small companies. In developed economies in Europe and elsewhere, there is a legal requirement of large companies that immediately after the payment of obligations to the government (paying taxes) settle their obligations to small and medium enterprises. The task is relevant to the creation of an adequate legal environment protecting small and medium enterprises.

It is also necessary to create the incentive policy to promote the external appearance of small and medium enterprises. Incentives would include simplification of administrative procedures for the export business and increase awareness of business conditions abroad. Lack of access to SME finance can be compensated by strengthening the existing support programs for small and medium enterprises. In this regard, it should work on further simplification of the accounting system and creating of financial and fiscal framework that will alleviate the difficulties faced by SMEs. Finally, it should encourage further innovative activities and providing assistance, training and consultancy services for managers and owners of small businesses in order to improve the method of entering foreign markets.

All these measures for stimulation of the internationalization of Serbian SMEs will take effect only if the synergistic approach of the economy and state representatives is achieved!

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