

FINANCIAL INCENTIVES TO THE DEVELOPMENT OF SMALL AND MEDIUM ENTERPRISES IN SERBIA

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ABSTRACT: Characteristics of Serbian economy are the following: high level of enterprises' inefficiency, three times larger import than export, decline in industrial production, large number of unemployed, high proportion of material costs in budget. Misunderstanding of entrepreneurship and small and medium enterprises is reflected in: the identification of entrepreneurs with artisans, attitude that small and medium enterprises generate entrepreneurship – and not vice versa, attitude that enterprise size provides automatic efficiency of micro and small enterprises in relation to the large ones, the existence of monopoly of large enterprises, attitude that small and medium enterprises are ideal solution to the problem of unemployment – only if they develop and grow, if they are market-efficient, only then they can generate new workplaces, unrealistic attitude – that economic conditions should be equal for all economic entities – which expresses fundamental ignorance of entrepreneurial development of economy.

KEY WORDS: small and medium enterprises, export, financial program...

1. INTRODUCTION

In the past years in Serbia, the payment system, Fund for Development of Serbian Government, from which the loans are directed towards large public enterprises, has functioned successfully. Apart from large banks, there were also small private banks. By the reform of banking system, after the year 2000, many banks have been put into liquidation, many foreign banks appeared, which have created credit policy by themselves. Although they are jurisdiction of the National Bank of Serbia, still we witness that they do not follow orders i.e. the rate of Euro in relation to dinar is much higher than it is published by the National Bank, interest rates are high. We can observe that not only the citizens as individuals are borrowing, but also the entrepreneurs, small and medium enterprises, large enterprises, i.e. they take extremely unfavourable loans, at high interest rates. If that tendency continues, there will be a situation that many people will not be able to repay their loans, i.e. the time will come for the banks to charge the mortgages, i.e. to sell the real estate that were mortgaged by the citizens or enterprises when taking the loan [5].

Problems in financial sector [6]:

- Lack of experience, especially in the evaluation and supervision of the operation of small and medium enterprises, with the result that financing of small and medium enterprises is considered too risky;
- Lack of supervision system in banks means that only highly secured short-term loans are approved;
- The fact that banks are undercapitalized means that they cannot approve long-term loans from their own sources;
- Lack of records of business operations of entrepreneurs and small and medium enterprises in the previous period in correlation with the fact that environment is changing rapidly makes the inherent risk of projects much higher than in comparable Western economy;
- Lack of government support measures for raising the level of banks' motivation to choose the higher interest in the financing of small and medium enterprises;
- Lending to small enterprises is very risky due to the high level of uncertainty with which small and medium

enterprises are faced (non-existence of qualified non-financial services that would reduce the impact of the risk of non-financial factors – good analysis of the market, competition, managerial weaknesses, weaknesses of organization and distribution of products and services);

- Commercial and credit banks do not have experience in operating with small and medium enterprises. Administrative costs of financing small and medium enterprises are very high, and size of loans is too small to cover these costs;
- Lack of transparency in evaluation of investments of small and medium enterprises and insufficient training of financial institutions in operating with small and medium enterprises;
- Inconsistency between banking instruments and terms for using the loan with different level of development and needs of small and medium enterprises;
- Attempts to use cheaply obtained loans for encouraging entrepreneurship and small and medium enterprises to rapid capitalization of the given investments at unreasonably high interest rates (10-30%) and
- Height of different types of loans securing, which exceed the amount of loans for 2-3 times.
- Problems with which small and medium enterprises are faced [8] :
- Small capital value per individual enterprise, low accumulation level;
- High level of banks' pledge as means to justify the risk;
- Low level of managerial capacity leads many small and medium enterprises into failure, especially those that arise from shares privatization, which only enhances banks' aloofness regarding small and medium enterprises;
- Changes in the environment, inflation, make the usual interest rate very high and long-term financing very risky;
- Lack of private capital is significant;
- Private property and its evaluation is often uncertain;
- Lack of small amounts for start-up capital;

This means that operating and survival of small and medium enterprises in our market is exclusively the merit of their owners, i.e. management personnel, and in a much smaller degree it is the merit of the state.

Limitations that occur with the financing of small and medium enterprises are [7, 8]:

1. Lack of long-term sources of funds;
2. Legislation;
3. Unpreparedness small and medium enterprises for cooperation with banks;
4. Lack of “good” projects;
5. Unreliable financial reports (balances);
6. Unreliable credit history;
7. Inadequate warranties;
8. Interest in short-term lending;
9. Interest in lending to large enterprises;
10. Unwillingness to partnership and risk sharing with small and medium enterprises;
11. (no) training of loan officers;
12. No data on participation of small and medium enterprises in the results of banking sector;
13. Job shops are denied the access to financial market;
14. Loans are expensive;
15. Lack of medium-term and long-term loans;
16. Non-standardized methodology of drafting a business plan;
17. Slow, complicated and expensive procedure of assessing business and loan ability;
18. Means of securing the credit.

What should the relation between the banking sector and small and medium enterprises be like:

- Small and medium enterprises should be the most important target groups to banks;
- It is necessary for that relation to be based on long-term basis;
- Full cooperation of banks and small and medium enterprises in risk management;
- Development is financed by own funds with the advances from customers and loans of suppliers;
- High and growing participation of short-term sources of financing;

- Above-average share of working capital;
- High level of writing-off of the fixed assets, obsolete technology;
- Job shops have the status of a physical person.

2. PROBLEMS OF THE SOURCES FINANCING OF SMALL AND MEDIUM ENTERPRISES

With the problem of the lack of sources of financing of small and medium enterprises, all the countries in transition were faced [1]:

- Banks are, after “family and friends”, the second significant source of financing;
- Illegal or partially illegal operating of small and medium enterprises is one of the largest brakes when approving the funds to small and medium enterprises by the banks;
- Non-functioning of the rule of law, as well as the lack of public information, automatically imposes a high interest rate;
- No country in transition has an ideal solution to financing of small and medium enterprises;
- Deposit base and ownership structure of banks are not suitable to financing of small and medium enterprises, while capital market still remains underdeveloped.
- Banks [1]:
- Mostly short-term and foreign currency deposits (up to 90 days) ;
- Lack of interest for small and medium enterprises (high fixed costs of loan processing, certain degree of business illegality, mortgages that are difficult to implement);
- The existing banks mostly serve large enterprises and population, banks with target market of small and medium enterprises almost as if do not exist;
- Ownership structure (foreign or private domestic) is not suitable to the engagement of banks in the sector of small and medium enterprises.

Table 1. Programs for small and medium enterprises [4]

	European Agency for Reconstruction	European Investment Bank	European Fund for Serbia
Loan sum:	15 million of Euros	40 million of Euros	18 million of Euros
Repayment period (grace period)	5 years (1 year)	12/15 years (3 year)	5 years (1 year)
Interest rate:	Below 8,14%	Below 7,04%	10-12 %
Number of loans approved:	More than 100	10	More than 400
Loan amount:	20.000 – 200.000 Euros	min. 200.000 Euros	max. 50.000 Euros

Source: National Bank of Serbia

The financing of small and medium enterprises still needs to be done through banks, with maximum respect for market mechanisms, ways to support the financing of small and medium enterprises need to be drafted with banks and not for banks, the state must support the financing of small and medium enterprises through appropriate regulation.

3. SMALL AND MEDIUM ENTERPRISES' ROLE IN EXPORT

The goals of small and medium enterprises should be the following [9]:

- Increase of sales and profit;
- Maximum use of production capacity;
- Increase of business security.

Reasons of small and medium enterprises for penetrating the international market should be the following:

- Small Serbian market;
- Small number of buyers for particular products.

Firstly, small and medium enterprises need to do the following:

1. Identify the possibilities

- Conduct research in the field, i.e. certain number of markets;
- Gather information on market size, data about the export, economic indicators, republic and local regulations;
- Sources of information: SIEPA, Regional Agencies for Small and Medium Enterprises, Chambers of Commerce.

2. Market choice;

- Focus on a several markets;
- Choose a market with sufficient potential, i.e. competitive advantage – price, quality.

3. Enter the market

- Distributors;
- Direct sales.

Rules for the selection of distributors [2]:

- Identify, choose a list, select, make a contact, negotiate and approve.
- Whether the agent is interested in the product and good reputation?
- Agent needs to believe that the product will be successful and to have confidence in efficiency and reliability of producer.
- Producer supports the work of the agent.

Direct sale can be:

- Direct supply for the client and managing all the contacts,
- Open sale,
- Sales over the Internet.

Priorities of one state's policy should be [2]:

- Promotional support for main markets;
- Information and advisory services;
- Development of export capacities of competitive small and medium enterprises;
- Export finances and insurance;
- Scheme of quality standard;
- Donor support in promotion of the trade.

Support to export capacities of small and medium enterprises [2]:

- Project „USAID“ for developing the enterprises in Serbia supports the export of small and medium enterprises that are the clients;
- Network of Regional Agencies for Small and Medium Enterprises provides direct advisory, information and training services for small and medium enterprises;
- Capacities of service provider of small and medium enterprises are improved through various projects.

4. INVESTMENT FUNDS IN THE FUNCTION OF DEVELOPING SMALL AND MEDIUM ENTERPRISES

Questions that stand before small and medium enterprises are:

- How to start the efficient production?
- How to keep the existing and win new markets?
- How to improve the quality of products, services?
- How to obtain as better position in the market?

Small and medium enterprises can start and develop efficient production by investing and by:

- Using own funds,
- Using borrowed funds,
- Commodity market:
 - Commodity loans
 - Leasing
 - Factoring
- Money market:
 - Friends' funds,
 - Banks' funds:
 - Short-term loans,
 - Long-term loans.
 - Funds from the Fund for Development of the Republic of Serbia:
 - Capital market.

Investment funds are the following:

- Non-banking institutions that carry out the mobilization of funds and investment of the same,
- Institutions with highly professional management,
- Expressed diversification of investments,
- Various objects of financing,
- Daily expression of prices.

Investment funds enable:

- Efficient allocation of funds by diversification of portfolios with taking care of internal and by law determined rules,
- Higher level of using long-term sources,
- Corporative control.

Investment funds take over the markets of banks and insurance companies because they provide:

- Relatively high returns,
- Low, i.e. medium level of risk,
- Liquidity of the securities.

Division of investment funds

1. According to the way of financing:

- Open funds,
- Closed funds,
- Interval closed funds.

2. According to the appearance of capital investment:

- In securities (shares, bonds),
- In real estate,
- Financial instruments.

Table 2. Schedule of total net assets in millions of US dollars by the fund type (I quarter 2003.) [3]

Regions	Total	Capital	Bonds	Money market	Balanced/mix	The rest
The world	11.209.715	3.998.834	2.642.127	3.196.809	902.504	212.859
America	6.667.505	2.681.705	1.309.977	2.251.059	399.976	24.878
Europe	3.476.434	928.941	1.055.849	731.018	440.908	54.136
Asia and Pacific	1.054.643	381.362	273.752	207.041	59.246	131.241
Africa	22.133	6.825	2.548	7.651	2.754	2.695

Source: www.arhiva.srbija.sr.gov.yu

Table 3. Number of investment funds [3]

Regions	I quarter 2003
World	51.150
America	13.972
Europe	27.960
Czech Republic	1.146
Poland	105
Romania	22
Hungary	91
Asia and Pacific	10.752
Africa	466

Source: www.arhiva.srbija.sr.gov.yu

Investment funds for development of small and medium enterprises [10]:

1. Provide long-term funds for the enterprise through the participation in ownership (capital share),
2. Participation in ownership can be:
 - In relation to time: limited or non-limited. y
 - In relation to the structure: minority or majority
3. A cooperation is established between the management of the fund and enterprise that guarantees an improvement of managing the enterprise, expansion and improvement of contacts with suppliers and buyers from the country and from abroad,
4. Identification of the problem,
5. Solving the problem,
6. Support to new developmental undertakings.

Investor could be:

- The state:
 - Funds from donation;
 - Funds from privatization;
 - Funds from budget.
- Territorial autonomy– Province;
- Unit of local self-government – municipality, city, city of Belgrade;
- International financial institutions;
- Banks;
- Citizens.

Each investment is preceded by analysis of information about:

- The existing plans and activities of enterprises;
- Management;
- Financial indicators;
- Financial projections.

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