

POLICY STRATEGY FOR SUPPORT TO THE DEVELOPMENT OF SMALL AND MEDIUM SIZED ENTERPRISES

1. Preamble

The Government of the Republic of Montenegro:

- Acknowledging the potential contribution of small and medium sized enterprises (SMEs) to economic growth, new employment creation, innovation, technology transfer and the attainment of social and economic cohesion in the Republic of Montenegro;
- Acknowledging current constraints to the development of SMEs, in particular low levels of business awareness and business skills, regulatory and administrative barriers, lack of access to affordable sources of medium and long term finance, inadequate access to sources of business and market information and limited availability of specialist business services;
- Acknowledging international best practices in the area of SME development and the provisions of the UN Declaration on Co-operation in the Development of SMEs in the Region of South East Europe, to which the Republic of Montenegro is a signatory;

Hereby:

Adopts this Strategy for Support to the Development of Small and Medium Sized Enterprises.

Consistent with the objectives of its 'Economic Development Strategy for 2002-2005' the Government of the Republic of Montenegro aims within the period of the current strategy:

1. To increase the number of registered private sector SMEs operating in the formal economy.
2. To achieve a greater diversity and integration of economic activity, increasing the proportion of SMEs based in production and non-trade services.
3. To significantly increase the proportion of small and medium sized enterprises relative to micro-enterprises in the total enterprise population.
4. To increase competitive SME activity in economic sectors where the Republic of Montenegro is currently reliant on imported goods and services and increase the contribution of SMEs to export earnings.
5. To increase the participation of domestic SMEs in foreign strategic alliances and joint ventures.
6. To increase the contribution of SMEs to GDP.
7. To increase the share of SMEs in total employment.

For the purposes of this strategy, the definition of a micro, small and medium sized enterprises follows the EU standard definition with respect to numbers of employees. Micro enterprises are defined as enterprises having fewer than 10 employees, small enterprises are defined as enterprises having fewer than 50 employees and medium-sized enterprises are defined as enterprises having fewer than 250 employees. On the basis of these definitions baseline data and quantitative targets for the strategy objectives will be established, pursuant to the reform of national accounting standards and statistics (section 7.)

3. Approach

The Government of the Republic of Montenegro recognises that it cannot work alone to achieve its SME development objectives. The successful implementation of the strategy requires the concerted and co-ordinated efforts of a range of stakeholders, including Government, international lending institutions, foreign donors, commercial banks and other financial institutions, non-governmental organisations, business representative organisations, business consultancy and advisory service suppliers and individual SMEs themselves.

At the same time, the Government recognises that its role in achieving the objectives of the strategy and its relationship to other stakeholders must evolve during the implementation period, focusing initially on measures to promote entrepreneurship and establish appropriate framework conditions for SME development. As the impact of these measures begins to be felt, Government involvement will focus increasingly on the provision of basic business education and information services that are not provided by the market.

4. Policy Priorities

4.1 Promoting Entrepreneurship

At the current time, levels of entrepreneurial activity in Montenegro are extremely low by international standards, reflecting the cultural legacy of the former command economy system and the subsequent effects of regional conflict and economic sanctions. In order to address this problem and to enable Montenegro to begin to compete in the international market economy, it is vital that steps are taken to promote entrepreneurship. In addition to a range of measures aimed at making it easier for citizens to start and operate businesses, this requires close co-operation with the media and other 'opinion-makers' to stress the benefits of entrepreneurship and private initiative as alternatives to employment in state owned companies and Government, and to create positive 'role models' for entrepreneurs. It is proposed:

- To investigate mechanisms for promoting entrepreneurship through partnership between government, business representatives, educationalists, the media and representatives of the free press, building on the work of the press club of Montenegro.
- In cooperation with educational institutions and the commercial banking sector, to organise a range of

- promotion projects, including the 'young people in business' competition
- To launch a specialist journal aimed at publicising SME success stories and promoting SME development opportunities

4.2 Promoting Business Skills

The emergence of a competitive SME sector requires not only the creation of new attitudes towards entrepreneurship, but also the development and application of modern business skills in areas such as management, finance and accounting, marketing and human resource development. Formal education has a crucial role to play in the development of such skills, providing people with the business concepts and techniques which can be applied and developed in the workplace. The Government of the Republic of Montenegro recognises that it has a crucial role to play in providing such education and supporting the emergence of private education initiatives at a variety of levels. Accordingly it is proposed:

- To investigate the possibility of introducing a basic business skills curriculum into tertiary education programmes throughout the Republic.
- To provide basic business education and training for start-up and early stage businesses. Wherever possible we will make use of international experience and expertise in the design and delivery of such programmes
- To actively promote and support the provision of high level management training, through the development of University business administration programmes. Early steps will be taken to establish the feasibility of developing joint Masters of Business Administration (MBA) programmes and / or correspondence courses with foreign Universities, thus encouraging Montenegrin students to obtain internationally recognised management qualifications.

4.3 Ensuring Fair Competition

In order to realise the full potential of entrepreneurship it is vital that businesses are able to compete on a fair and equal basis. Experience from other countries shows clearly that where businesses are protected from competition, either by misuse of monopoly powers or regulatory or tax avoidance, this translates directly into lower quality goods and services and higher end prices to consumers. Solving the problem of unfair competition is therefore vital in order to provide a basis for sustainable long term growth, ensuring that the best businesses survive and compete in domestic and international markets. The Government of Montenegro is committed to this end and has already embarked on an ambitious but achievable plan to combat the main source of unfair competition, the grey economy. In addition to relieving the overall

burden of business regulation and administration during the strategy period (below) it is proposed:

- To implement rigorous programmes of education for public officials engaged in the implementation and administration of new legislation, including the new enterprise and tax laws
- To introduce new administrative procedures in relation to enterprise legislation and regulations, design to foster increased compliance and ensure greater consistency in implementation and enforcement
- To introduce more stringent monitoring and evaluation procedures in respect of new and existing legislation.

4.4 Reducing Regulatory and Administrative Barriers to Business Development

The Government of the Republic of Montenegro recognises that it has an important role to play in regulating private business activity. It also recognises that excessive, poorly drafted and rapidly changing regulation can stifle entrepreneurship and impair the development of the economy, increasing the administrative burden on businesses and encouraging flight into the informal sector. The Government is therefore committed to achieving an appropriate balance of regulation, consistent with its social policy obligations and the need to promote economic transition and growth, and recognising that the costs of compliance for small firms are proportionately higher than for large firms. It is proposed:

- To complete current work on streamlining business registration procedures. Within the framework of the new law on business organisation, systems will be put in place to significantly reduce the average registration period for new businesses.
- To undertake a systematic review of licensing and permitting requirements, in order to identify areas where current regulations and their administration can be streamlined in accordance with international best practices.

4.5 Simplifying the Business Taxation System

A simple and transparent tax system that recognises the disproportionate costs of compliance faced by SMEs is an essential prerequisite for growth in a market economy. For this reason, the Government of the Republic of Montenegro has already taken significant steps towards simplifying taxation measures that impact on SMEs, including the revision of excise taxes and the revision of taxes on personal income and corporate profits. Equally importantly, through the unification of the tax administration system under the Ministry of Finance, steps have been taken to streamline the operation of the tax administration system to ensure greater consistency and transparency. During the period of the strategy it is proposed:

- To examine the case for further revisions to tax laws aimed at reducing the burden for SMEs and encouraging significantly improved levels of voluntary compliance. In developing new tax measures, including potential tax breaks, reduced thresholds, streamlined assessment and payment mechanisms etc, we will pay particular attention to lessons learned from OECD best practices in this area.
- To overhaul and revise current laws and regulations governing employment taxation and to bring this more closely into line with other 'competitor' economies.

4.6 Encouraging the Formation of Private Business Associations

The Government of the Republic of Montenegro recognises that in developed market economies, business associations play a key role in articulating the needs of SMEs and lobbying government for change. Sectoral business associations also have a key role to play in disseminating information to their members, providing specialist education, promoting internationalisation and establishing and maintaining quality standards, frequently reducing the need for government regulation. In order to promote the development of private business associations, the Government proposes:

- To co-operate with existing business associations and to encourage the development of new business associations which can make a reasonable claim to representing the interests of businesses in their sector and / or area.
- To seek ways of incorporating legitimate private business associations into government policy and decision-making processes at national and local levels.
- To support further work in this area by international donor organisations and to be responsive to proposals emerging from this work.

4.7 Increasing Access to Business Information

Trends from developed market economies suggest that over the last decade, access to information (about new products and processes, competitors, trends, new markets and customers) has become increasingly important in determining competitiveness. This has left businesses in Montenegro with a double disadvantage, having lost markets previously established within the Former Republic of Yugoslavia and endured a prolonged period of economic sanctions during which access to new international markets was not possible. As a consequence, businesses in Montenegro must make up ground quickly if they wish to compete successfully for domestic and foreign markets. In order to assist businesses in this process, Government proposes:

- To establish a network of Regional Business Information Centres (RBICs). During the strategy period, seven centres will be created, enabling businesses throughout the country to obtain access to information without the need to travel large distances. The centres will be located in local government offices and will provide basic information to businesses with the aim of making it simpler to register a business and operate legally and to identify sources of SME finance and specialist technical advice, for example, business planning. The centres will also provide consultation rooms and internet access for registered customers.
- To establish a **European Information and Correspondence Centre (EICC)**. The EICC will be established in Podgorica and will provide further services to businesses in the form of information on European standards and markets and the organisation of European trade events, including inward and outward trade missions. The EICC will disseminate information at regional level through the proposed network of RBICs.

4.8 Increasing the Supply of Business Services

By comparison to more developed market economies, the supply of business services in the Republic of Montenegro is extremely limited. Services such as accountancy, tax planning, legal advice, information technology and management consultancy are nevertheless crucial in assisting businesses to become established and grow, as well as being important sources of economic activity and employment in their own right. Accordingly, the Government of Montenegro is committed to encouraging the development of business services. It is proposed:

- To continue to support training programmes supported by international donor organisations aimed at training private sector business service trainers and specialists. Existing programmes in this area will be reviewed to establish their impact and new programmes addressed to gaps in current provision.
- To support proposals by the European Agency for Reconstruction and Development to provide training to private business service providers through the EBRD Turn Around Management programme.
- To train local government officials employed in the RBICs to provide customer-oriented information services with respect to government laws and regulations impacting on SMEs. During the early stages of the implementation of this strategy, particular emphasis will be placed on informing business customers about the new commercial and taxation laws. Advice relating Government laws and regulations will be strictly confined to issues of compliance.

4.9 Facilitating Access to Affordable Finance

The Government of the Republic of Montenegro recognises that lack of access to affordable sources of finance is a major constraint for SMEs that wish to invest and grow, particularly start-up and early stage businesses that need to borrow for periods in excess of one year. The Government also recognises that in the transition to a market economy, the primary role of the State should be to facilitate the supply of private finance to businesses, rather than to act as a lender its own right. Accordingly it is proposed:

- To continue efforts to restructure the commercial banking sector, with the aim of encouraging greater competition and increasing the volume and quality of domestic SME loans in accordance with international lending practices and prudential requirements.
- To cooperate with international lending institutions which express a willingness to establish new credit lines in the Republic of Montenegro. Special efforts will be made to attract internationally supported financial intermediary programmes that simultaneously build the capacity of commercial banks and encourage greater lending competition.
- To promote increased competition in the supply of micro-finance through further cooperation with international lending institutions and non-governmental organisations active in this area
- To investigate the feasibility of establishing new forms of SME and micro-finance, addressed to current and emerging gaps in market provision. Early efforts will focus on the demand for and feasibility of private mutual guarantee associations and public guarantee institutions as mechanisms for leveraging increased SME lending through the commercial banking sector.
- To create enabling legislation and efficient taxation instruments to encourage the formation and growth of new SME and micro-finance institutions.

5. Implementation, Monitoring and Evaluation

Co-ordinating the implementation of this SME development strategy and monitoring its progress are primary responsibilities of the Government's 'Agency for the Development of SMEs' (ADSME), established in December 2000. In order to fulfil these responsibilities, it is envisaged that ADSME will work increasingly closely with emerging private sector representative organisations in Montenegro to establish a sound understanding of SME development needs. Government will also create mechanisms for ensuring that ADSME is able to effectively coordinate the work of all line Ministries responsible for implementing parts of the strategy and international donor organisations active in the field of SME development.

In order to ensure that ADSME is able to perform its role effectively and to ensure that Government, SME stakeholders and the citizens of the Republic of Montenegro

are properly informed of progress in the achievement of the strategy, it is further proposed:

- To overhaul and update national statistics relating to businesses, in accordance with European and OECD national accounting standards. This will allow for more accurate and timely information on inter alia new business formation rates and the contribution of SMEs to GDP, employment and export growth.
- To facilitate the development of an SME advisory council (comprised of key representatives from legally operating SMEs) to liaise with ADSME over the implementation and monitoring of the strategy and to assist Government in assessing ADSME's efficiency and effectiveness.

Within the framework of this strategy, ADSME will be responsible for drafting annual action plans containing specific actions that it will undertake, implementation responsibilities, outputs and a detailed delivery timetables. Government will undertake an independent mid-term evaluation of the ADSME's performance, based on this Strategy and delivery against the year 1 and 2 action plans.