

Support Diversification for Micro, Small and Medium Size Enterprises in Zemgale Region

Zanete Gruzina¹, Mg.oec., lecturer; **Andra Zvirbule-Berzina**, Dr.oec., assoc. professor
Latvia University of Agriculture, Faculty of Economics

Abstract. The paper presents the concept of support diversification for development of micro, small and medium size enterprises (MSMEs) in Zemgale region, Latvia. Financial, advisory, and educational support is crucial for the establishment and development of micro, small and medium size enterprises worldwide. The World Bank, the European Commission, and governments have all showed an increased interest in financing and supporting MSMEs. The research is focused on discussion and classification of support available for the establishment, and growth and development of micro, small and medium size enterprises in Latvia. Cluster analysis groups 22 local municipalities of Zemgale region into 4 clusters, and the authors suggest to diverse support according to specific needs of region and enterprises in each cluster. In the clusters that link territories with low number of micro enterprises per 1000 capita, it is necessary to stimulate the establishment of new micro enterprises through programmes like Promotional Programmes Office ALTUM Start Programme, Micro Lending Programmes as well as education and training. In contrast, in clusters with high number of micro enterprises per 1000 capita but low number of small and medium size enterprises, it is important to stimulate the growth of micro enterprises into small, medium and large enterprises through Competitiveness and SME Growth Loan programmes.

Key words: financial support, support diversification.

JEL code: E02

Introduction

The firm size plays an important role in entrepreneurship. Micro, small and medium size enterprises (MSMEs) face difficulties and problems, when trying to survive and develop. According to Schiffer and Weder, there are 3 main problems that small and medium size enterprises are facing: tax policy, access to finance, and inflation. Large enterprises are more concerned about policy instability, tax policy, and inflation (Schiffer M., Weder B., 2001). Access to finance is one of the problems that the European Commission is concerned about. The European Central Bank conducted survey between 22 August and 7 October 2011, covering a sample of 8316 firms in the euro area. According to the survey results, external financing needs of MSMEs have slightly increased between April and September 2011. The survey results show that access to bank loans has deteriorated at the same time. On balance, firms' opinion about the availability of bank loans has decreased by 5 percentage points reaching 14%. Moreover, the survey results point to slightly lower rates of success when applying for a loan. Meanwhile, the percentage of respondents reporting "access to finance" as their main problem was unchanged and stood at 16% (Report on the Results..., 2011). Because financial support is limited, it is important to diverse it according to the needs of specific region and enterprise. In this paper, the authors take into account not just financial support offered for MSMEs but also consultations, knowledge sharing, and advisory services for MSMEs.

The **aim of the research** is to analyse possibilities of support diversification for micro, small and medium size enterprises in Zemgale region. Three **research tasks** are set up to reach the aim:

- 1) to describe the role of micro, small and medium size enterprises;
- 2) to classify and describe support that is available for the establishment, and growth and development of micro, small and medium size enterprises in Latvia;
- 3) to analyse opportunities of support diversification for micro, small and medium size enterprises through cluster analysis of Zemgale region.

The **research methods** are monographic descriptive, analysis, synthesis, statistical methods, and cluster analysis. The paper presents the classification of support that is available for MSMEs into two main groups: 1) support for the establishment of MSME and 2) support for the growth and development of MSME. Cluster analysis is used to group 22 local municipalities of Zemgale region into four homogeneous groups, so that the authors can suggest different strategy for each group of local municipalities. Cluster analysis is based on 4 socio-economic indicators from the year 2009: number of micro size enterprises per 1000 capita, number of small size enterprises per 1000 capita, number of medium-size enterprises per 1000 capita, and specially supported territory status. If a territory has the status of specially supported territory, it shows that there are long-lasting negative social and economic processes in this territory.

1. Role and importance of micro, small and medium size enterprises

Micro, small and medium size enterprises play an increasing role in economy, but there is not common understanding of the term micro, small and medium size of enterprise. The number of employees and financial data

¹ E-mail address: zanete.gruzina@llu.lv

Table 1

Share of micro, small and medium size enterprises in the number of enterprises, employment and number of employees per enterprise in the EU countries average, 2008

Enterprises	Micro	Small	Medium	MSME	Large
Number of enterprises					
Number	19 058 000	1 424 000	226 000	20 709 000	43 000
%	91.8	6.9	1.1	99.8	0.2
Number of employees					
Number	39 630 000	27 652 000	22 665 000	89 947 000	43 414 000
%	29.7	20.7	17.0	67.4	32.6
Number of employees per enterprise					
Number	2.1	19.4	100.3	4.3	1006.1

Source: authors' calculations based on the *European SMEs under...*, 2010

Table 2

Number of micro, small and medium size enterprises in Latvia and their growth rates in 2004-2009

Year	Micro enterprises	Growth rate, %	Small enterprises	Growth rate, %	Medium enterprises	Growth rate, %
2004	89230	-	10062	-	2006	-
2005	95879	7.45	10832	7.65	2125	5.93
2006	105603	10.14	11193	3.33	2363	11.20
2007	113288	7.28	12745	13.87	2546	7.74
2008	113008	-0.25	12482	-2.06	2546	0.00
2009	115654	2.34	10122	-18.91	2037	-19.99

Source: authors' calculations based on *Mikro, mazo un videjo uzņemumu...*, 2011

(turnover, assets, investment, or capital) are the most common way to define size groups of micro, small and medium size enterprises. According to the Commission Recommendation of 6 May 2003, the common definition used by 27 Member States define, that:

- micro enterprise is an enterprise, which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million;
- small enterprise is an enterprise, which employs fewer than 50 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 10 million;
- medium enterprise is an enterprise, which employs fewer than 250 persons and which has an annual turnover not exceeding EUR 50 million, and/or an annual balance sheet total not exceeding EUR 43 million (MSME definition, 2003).

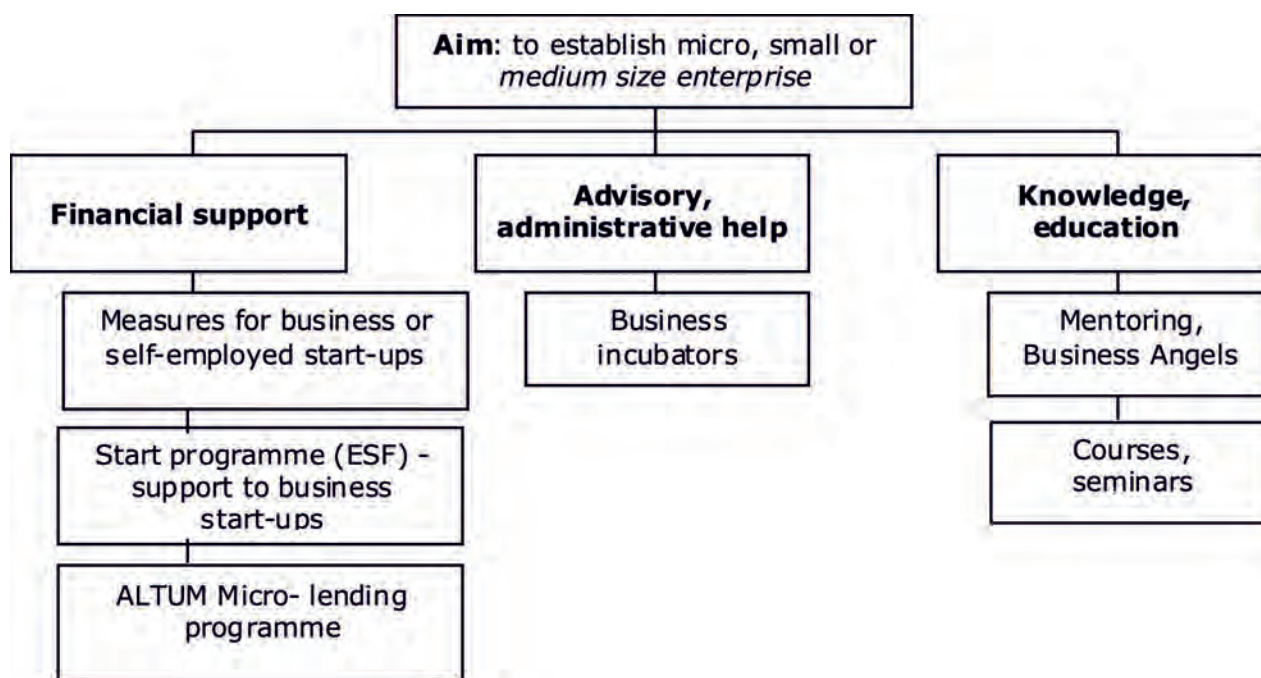
According to this definition, around 99.8% of enterprises in the European Union countries are micro, small or medium (Table 1).

Around 92% of all enterprises in the EU are micro (up to 9 employees), and in total these enterprises employ over 39 million people, with the average of 2 employees per enterprise. Over 1.4 million or 7% of all enterprises can be classified as small. Yet, they employ 21% of all employees in the EU, with the average of 19 employees per enterprise. Medium enterprises

comprise only 1% of all enterprises, but they employ 17% of all employees. In total, micro, small and medium size enterprises constitute 99.8% of all enterprises, employing 67% of all employees in the EU, with the average of 4 employees per enterprise. In the EU Member States, the share of MSMEs is important, thus, it is essential to establish support system for the development of these enterprises.

In Latvia, tendencies of MSMEs development are similar to the EU. Table 2 shows the statistics of MSMEs in Latvia during the years 2004-2009.

As shown in Table 2, the number of micro enterprises in Latvia experienced a steady growth during the years 2004 and 2007, but during recession, they experienced a slight drop of 0.25%. During recession, the Ministry of Economics of the Republic of Latvia took immediate action and developed the Microenterprise Support Concept. According to the Microenterprise Support Concept, the main tasks to develop microenterprises are as follows: decreased establishment costs, simple bookkeeping, friendly tax policy, and simple access to finance (Microenterprise Support Concept, 2009). These actions were effective and the number of micro enterprises increased by 2.3% in 2009 compared with the year before. Small and medium size enterprises have similar tendencies - until 2008, the number of small and medium size enterprises experienced a slight annual growth of 10% on average. In 2008, the number of small



Source: authors' construction

Fig. 1. Support available for the establishment of micro, small and medium size enterprises

enterprises dropped by 2%, while the number of medium enterprises stayed stable. Both, the number of small and the number of medium size enterprises experienced impressive decrease during 2009- respectively by 19% and 20% due to recession. Because of economic problems, many small and medium size enterprises bankrupt or were forced to decrease their size. In total, the number of MSMEs decreased by 0.2% in 2009 compared with 2008 due to decline in the number of small and medium size enterprises and the increase of the number of micro enterprises.

2. Support for the development of MSMEs in Latvia

In Latvia, the available financial support for micro, small and medium enterprises can be classified into two groups: 1) financial support that is available to establish MSME and to ensure the first years of its work; and 2) financial support that is available for the existing MSMEs that are aiming at growth and development. Figure 1 shows support that is available for establishing MSMEs.

To establish a micro, small or medium size enterprise, three types of support are available: financial support, consultations and administrative help, and knowledge sharing and education. There are three main sources of financial support for MSMEs.

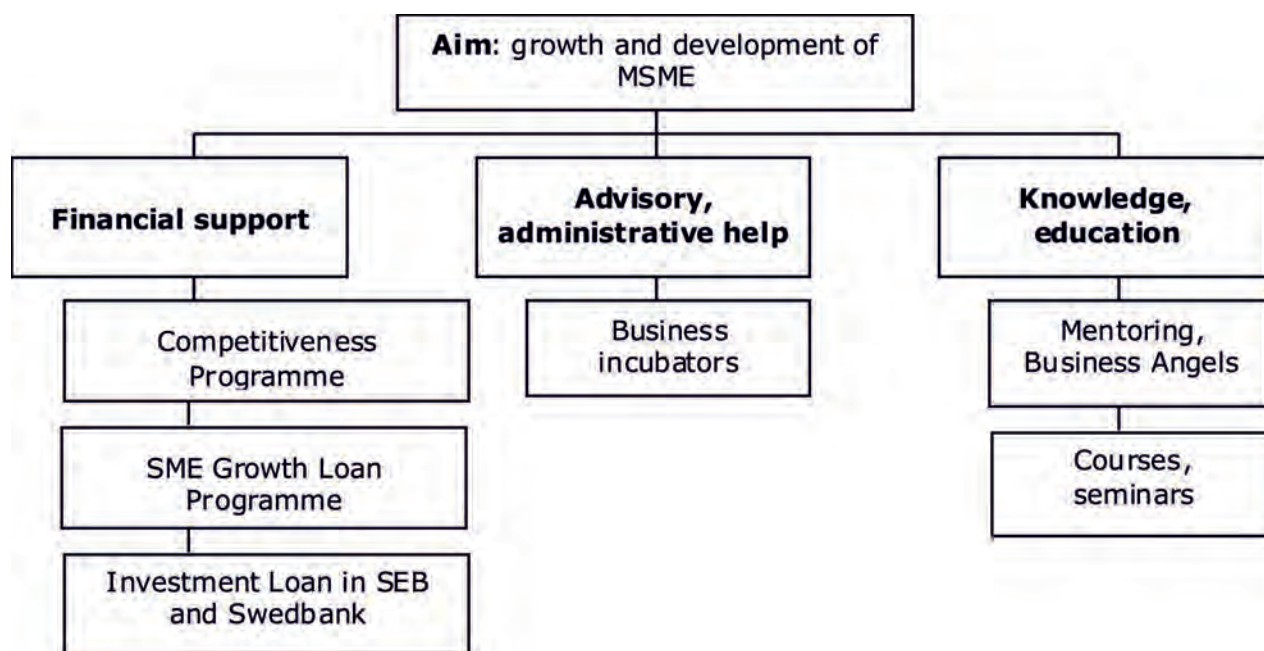
- **Measures for business or self-employed start-ups** - administrated by the State Employment Agency and offering training and support up to LVL 2000 for the development of business plans to registered unemployed persons (Pasakumi komercdarbibas..., 2011).
- **Start programme (ESF) - support to business start-ups** is administrated by the Promotional

Programmes Office ALTUM. The programme provides the business start-ups and newly established companies with an all-embracing support, i.e. consultations, training, and financing in the shape of loans and grants for starting the business. Consultations, loans up to LVL 54 thousand and grants up to LVL 2 thousand are available (Start programme..., 2011).

- **Micro-lending programme** is administrated by ALTUM and the overall objective of the programme is to improve access of micro enterprises (up to 10 employees) and self-employed persons (individuals – economic operators) to micro loans for setup and development of business activities. Loans are intended for the implementation of business plans – both for investments and working capital – and the loan volume is up to LVL 10 thousand, with fixed interested rate from 5% to 8% per annum and loan maturity up to 5 years (Micro Lending..., 2011).

There is one main source of consultations and advisory help and two sources of sharing knowledge and education.

- **Business incubators** are aimed to promote new, viable and competitive businesses, providing them with the necessary environment for business and advisory services. Business incubation is a unique and flexible business development process – a combination of infrastructure and personnel, designed to help develop new and small businesses by supporting the early stage of development with daily consultations based on business development issues (Biznesa inkubatori, 2011). There are five business incubators established in each region of Latvia.



Source: authors' construction

Fig. 2. Support available for the growth and development of micro, small and medium size enterprise

- **Mentoring and Business Angels** - movement of mentoring and business angels is becoming popular in Latvia. Both mentors and business angels are experienced business people who are willing to share their knowledge and experience with new and inexperienced start-ups.
- **Courses and seminars** - Investment and Development Agency of Latvia (LIAA) is offering several training sessions and courses for business start-ups and providing information about available support.

It is important that financial support is available not only during the establishment of MSME but also for its growth and development. In Figure 2, the authors summarise support available for the growth and development of micro, small and medium size enterprises.

Three main sources of financial support are available for the growth and development of micro, small and medium size enterprise.

- **Competitiveness Programme** grants loans to the businesses registered in Latvia with economically feasible business plans that cannot access the financing of the credit institutions due to increased risks they present. The total loan amount per one entrepreneur may not exceed LVL 7.5 million. Mostly, the loans are intended for implementation of the projects of the processing businesses and entrepreneurs attracting the financing of the EU Structural Funds' grant programmes (Competitiveness Programme, 2011).
- **SME Growth Loan Programme** finances small and medium enterprises and cooperative unions providing agricultural services that have economically feasible action plans but cannot access the financing due to high risk they present. The programme is financed by the European Investment Bank. Two types of loans are available - for investments and for working capital (including credit lines). The working capital

and investment loans taken together may not exceed LVL 300 000 for one entrepreneur (SME Growth..., 2011).

- **Investment Loan in SEB and Swedbank** in cooperation with the European Investment Fund. Investment loan is aimed to grant loans to small and medium size enterprises in Latvia. It is possible to finance investments in movable and immovable fixed assets and working capital to promote core expansion and development using loan of the European Investment Fund (Eiropas investiciju..., 2011).

For growth and development of MSME, it is still possible to use help and advice of business angels and mentors as well as it is possible to use services of business incubators if the business is established not earlier than 2 years before entering incubator.

3. Support diversification for the development of micro, small and medium size enterprises in Zemgale region

Zemgale region consists of 20 local municipalities and 2 cities, and each of 22 territories shows different development indicators. Therefore, the authors suggest to diversify financial support available for MSMEs to ensure development of all local municipalities. To diversify the support system, it is important to group 22 territories into few clusters. This allows to group homogeneous territories into groups and afterwards to work with each group separately. The authors use cluster analysis with 4 factors: number of micro enterprises per 1000 capita in 2009; number of small enterprises per 1000 capita in 2009; number of medium size enterprises per 1000 capita in 2009; and specially supported territory status. Specially supported territory status is used to describe territories with long lasting negative social and economic processes.

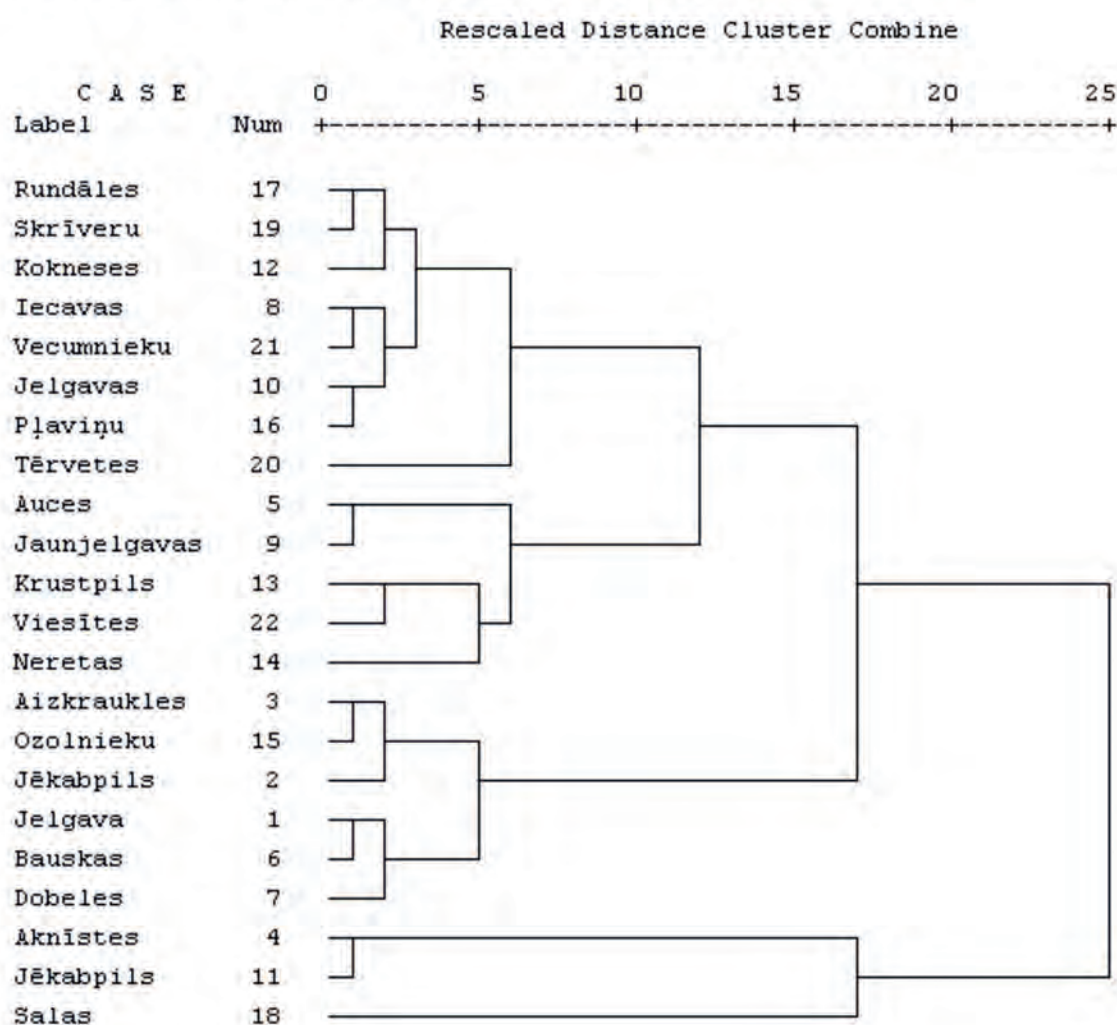
Table 3

Description of clusters according to the cluster analysis

Criteria	Clusters			
	1	2	3	4
Average number of micro enterprises per 1000 capita	35.4	50.1	39.5	94.2
Average number of small enterprises per 1000 capita	1.6	1.7	3.7	1.5
Average number of medium enterprises per 1000 capita	0.2	0.3	0.8	0.6
Specially supported territories	-	Auce, Nereta, Viesīte, Krustpils, Jaunjelgava	-	Sala, Jekabpils, Aknīste

Source: authors' construction

Dendrogram using Average Linkage (Between Groups)



Source: authors' construction

Fig. 3. Dendrogram using average linkage for local municipalities in Zemgale region

Local municipalities and cities are grouped in 4 clusters (Figure 3). Cluster 1 consists of Rundale, Skrīveri, Koknese, Iecava, Vecumnieki, Jelgava, Plavinas, and Tervete local municipalities. Cluster 2 consists of Auce, Jaunjelgava, Krustpils, Viesīte, and Nereta local municipalities. Cluster 3 consists of Aizkraukle, Ozolnieki,

Bauska, and Dobeles local municipalities, and Jelgava and Jekabpils cities. Cluster 4 consists of Aknīste, Jekabpils, and Salas local municipalities. As shown in dendrogram, the closest connection between data is in Cluster 1 as linkages between local municipalities are close. Opposite is Cluster 4, where linkages between Aknīste, Jekabpils,

and Sala local municipalities are not as close. According to the information in dendrogram, the authors describe each cluster in Table 3.

Cluster 1 links territories with the average of 35 micro enterprises, 2 small, and 0.2 medium enterprises per 1000 capita. Cluster 2 links territories with the average of 50 micro enterprises per 1000 capita, 2 small, and 0.3 medium enterprises per 1000 capita; besides there are 5 specially supported territories in this cluster. Cluster 3 merges territories with the average of 50 micro enterprises per 1000 capita, 4 small, and 0.8 medium enterprises. Cluster 4 contains three local municipalities with very high number of micro enterprises per 1000 capita - 94, which is almost 3 times more than in Cluster 1 and Cluster 3; however, there are 2 small and 0.6 medium size enterprises per 100 capita, so all 3 local municipalities are specially supported territories.

Conclusions, proposals, recommendations

Access to financial support is one of the main problems for micro, small and medium size enterprises. Therefore, the authors of the article suggest that according to the analysis of Zemgale region it is possible to diversify the available support:

1. Cluster 1 links territories with the lowest number of micro enterprises per 1000 capita, average number of small enterprises, and lowest number of medium size enterprises. In these territories, it is important to stimulate the establishment of new micro and small enterprises, and also to stimulate the growth of existing micro and small enterprises into medium and large size enterprises. It is necessary to stimulate the establishment of new micro enterprises through programmes like ALTUM Start Programme, Micro Lending Programmes as well as education and training.
2. Cluster 2 is characteristic with a high number of micro enterprises per 1000 capita but lower number of small and medium size enterprises. Because of high share of micro enterprises, there are 5 local municipalities, which are specially supported territories with negative social and economic environment. It is important to stimulate the growth of micro enterprises into small, medium and large enterprises through Competitiveness and SME Growth Loan Programmes.
3. Cluster 3 merges territories with the second lowest number of micro enterprises and the highest number of small and medium size enterprises per 1000 capita. High share of small and medium size enterprises, which employs between 11 and 249 employees ensures that territories do not have negative social or economic situation. In this cluster, it is important to stimulate the establishment of micro enterprises through programmes like ALTUM Start Programme, Micro Lending Programmes as well as education and training, yet, at the same time it is important to keep small and medium size enterprises developed, since they ensure high employment.

4. Cluster 4 contains three local municipalities with a very high number of micro enterprises per 1000 capita but at the same time, there is a very low number of small and medium size enterprises. The high share of micro enterprises leads to the fact that all 3 municipalities are specially supported territories with negative social and economic indicators. The main task in this cluster is to stimulate the growth of the existing micro enterprises into medium and large enterprises. It is necessary to stimulate growth and development of existing micro enterprises, rather than establishment of new micro enterprises.

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