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## Small- and medium-sized enterprises in Latvia: economical and social aspects

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**Abstract:** This publication deals with the social and economic situation of the small- and medium-sized enterprises (SME) in Latvia. It includes information about the state economic policy and the goals of its further development. There is discussion of conditions favouring the development of the SME, as well as existing problems. Generally accessible statistical data is given about the present environment of the entrepreneurial activity in relation to the SME. For characteristics of the situation in Latvia parallels are drawn with the development of SME and the existing situation in the EU countries. Analysis is given of the performed actions in connection with Latvia's integration in the European Union.

**Keywords:** small- and medium-sized enterprises (SME); social and economic policy; business development policy; state support; integration in the European Union.

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## **1 Economic goals and priorities of the Latvian government**

The economic policy goal of the government is sustainable and balanced economic and social development. To reach this goal a stable macroeconomic environment is maintained in Latvia and structural reforms that are directed to growth and deeper integrities into the EU are carried out.

The government of Latvia realises a liberal foreign trade and foreign investment policy. The law guarantees protection of foreign investment, foreign nationals may freely repatriate their profits and capital, and equal terms are provided to domestic and foreign entrepreneurs. The further liberalisation is linked with economic interests of Latvia – integration into the EU and implementation of commitments in the WTO.

The medium-term aims of the fiscal policy of the government are:

- to implement fiscal policy oriented on stable macroeconomic growth
- to ensure that the fiscal deficit of the consolidated general budget does not exceed 3% of GDP; in 2004 it is planned to bring down the fiscal deficit to 2% of GDP
- to verify the usefulness and efficiency of the whole budget, to raise efficiency and rationality of use of budget resources
- by promoting exports and ensuring economic growth to gradually bring down the current account deficit.

The government actively fights tax evasion. The priorities in this field are: fighting all kinds of smuggling, VAT fraud and eradication of the 'envelope' salaries. The State Revenue Service is implementing measures to perfect its taxpayer service with the aim to ensure better tax collection and reduce the need to apply penalties.

The law 'On Establishment of the Anti-Corruption Authority' gained effect on May 1st, 2002. The government has made the commitment to ensure efficient work of the anti-corruption authority by reinforcing its independence, granting bigger investigative powers and attracting international experts as well as wider involvement of the society in fighting corruption.

'The Procurement Supervision Bureau' started to operate in 2002 having a wide authority to control purchases made by central and local governments. The government has promised to ensure complete transparency of the state and municipal procurement procedure by publishing all information about purchases, including the submitted offers, decisions of the evaluation commission, concluded contracts, their amendments and annexes.

Targeted work at the improvement of business environment is carried out introducing requirements of *acquis communautaire*, reinforcing the system of property rights protection, introducing the 'Commercial Law' and implementing and updating the Cabinet of Ministers approved 'Action Plan to Improve Business Environment'. The *Action Plan* has assisted to reach a considerable improvement of entrepreneurial environment by lessening administrative barriers, streamlining tax administration, customs and border crossing procedures, providing wider access to information and better protection of investors. The *Action Plan* is regularly updated with new activities and 91 task of 106 activities mentioned in the *Action Plan* in 1999 have already been accomplished. The Cabinet of Ministers approved the latest *Action Plan* on July 29th, 2003.

The *Commercial Law* gained effect on January 1st, 2002 marking a fundamental reform of the business environment. It systematises in one place all the issues regulating business that until now were scattered in various legislative acts and will revoke series of outdated legislative provisions and will establish a safe system of protection of creditors and minority shareholders.

The *Draft Fundamental Guidelines for the Development Policy of Small and Medium-Sized Enterprises of Latvia* was submitted to the Cabinet of Ministers on October 27th, 2003. The key task of this document is to promote sustainable development of SME on the whole territory of Latvia, to ensure a favourable and encouraging environment for development of business ideas, creation of new enterprises and promote the general growth and competitiveness of SME. The new development programme of small- and medium-sized businesses will reinforce the guidelines in 2004–2006, which is currently being developed. Implementation of the programme will be connected with the utilisation plans of the financial resources of the EU Structural funds.

The *Mortgage and Land Bank* of Latvia has an important place in the system of state support. The Programme of Crediting SME of Latvia is implemented through this bank. In 2000–2002 the Mortgage and Land Bank of Latvia received state guarantees to support SME projects for the amount of ten million LVL. In November 2002 the Cabinet of Ministers passed the decision on further development of the SME crediting programme for the next three years (second phase) and provided state guarantees to the bank in the amount of 20 million LVL.

Also the Latvian guarantee agency (LGA) is becoming an efficient mechanism of SME support. In 2003 the LGA received 250,000 LVL of state budget funds to support its work. The LGA provides guarantees for the starting businesses and for the support and development of the business activity.

*Consulting Support Programme for Starters of Commercial Activity* has been developed. The aim of the programme is to encourage creation of new companies and to develop the existing ones, gradually reinforcing their position in the market and in the closest perspective – also in the single EU market. The total funding earmarked for the programme in 2003 was 80,000 LVL, 40,000 are allocated from the state budget

resources (50% of total costs). The Ministry of Economics plans to work out a similar programme for consulting small- and medium-sized enterprises in 2004.

The *Latvian development agency (LDA)* is charged with the task to promote foreign direct investments. LDA provides services to all the investment projects coming from foreign countries, however a clear priority is to identify and place foreign direct investment project targeted at promotion of exports, creation of knowledge and produces with a high added value. The target sectors are IT&T, electronics, financial services and administrative auxiliary functions, transport and logistics, biotechnologies. To implement the *Development Concept of Foreign Economic Representative Offices of Latvia* the LDA has opened or will soon open five new representative offices in foreign countries – Germany, Russia, UK, Sweden, France.

The National System of Quality Assurance has been set up in Latvia. It comprises the legislative base and institutional infrastructure. Almost all the relevant EU directives have been transposed.

In 2002 the *Latvian National Accreditation Office* signed the agreement with the European accreditation organisation on multilateral recognition of accreditation of testing and calibrating laboratories, products, quality systems and personal certification institutions, which has even more reinforced the system of Latvian accreditation.

Latvia has reached a substantial progress in the area of implementation of the competition policy. The legal base has been created and a supervision institution – the *Competition Council* has started to work successfully.

With the adoption of the law *On Regulators of Public Utilities*, the establishment of a two-tier public utilities regulation system was started in 2001. The first level regulator – public utilities commission (PUC) – regulates public services on the national level. Second level regulators or local government regulators are in charge of regulation of respective sectors on the territories of their local governments.

The market of voice telephony and leased lines is open for competition from 2003. The *Public Utilities Commission* has issued approximately 200 licences to individual telecommunications operators, mainly for data transmission and internet services.

Creation of market conditions in the sectors of electricity and liberalisation of the gas market are important government priorities.

Opening of the electricity sector proceeds gradually. All energy users of Latvia should be provided opportunity to freely choose their electricity suppliers. The *Public Utilities Commission* in preparation for liberalisation of the electricity market has developed tariff estimation methodologies for each technological phase of electricity supply, i.e. generation, transmission, distribution and sales. According to the new methods, the approved tariffs that gained effect on January 1st, 2004 will eliminate cross-subsidies and encourage qualified users to benefit from options available.

The *Gas Market Liberalisation Concept* approved by the government foresees creation of legal preconditions for the third party access and identification of the status of qualified users of gas in line with *aquis communautaire*, foresees regulations of gas distribution, supply and storage tariffs and also regulation of gas prices for the connected users. Price difference between user groups singled out depending on the quantity of consumed gas should be economically justified and correspond to market situation.

On August 3rd, 2003 the Cabinet of Ministers approved State Strategy on Privatisation of State and Local Governments Property. The strategy identifies optimal directions and approaches to complete privatisation. The government has committed to complete privatisation of the remaining enterprises trying to preserve the maximal number of jobs and gaining maximal revenues for the State Treasury.

Respecting public opinion, Latvian power company 'Latvenergo' as a single company will remain in the ownership of the state. At the same time it must be noted that the European Parliament and the Council Directive 2003/54/EC of June 26th, 2003 on single conditions in the internal electricity market requires separation, organisationally and for the purposes of decision-making, of the transmission system operators in a vertically integrated company in the form of a legally independent entity from other activities not linked with electricity transmission. At the same time the Directive does not require separation of the property rights on transmission system assets from the vertically integrated company.

The government carries out different measures to improve the situation in the area of employment. These measures are included in the annual national employment plan (NEP). NEP for the year 2003 contains a list of 56 activities for the amount of 22.5 million LVL. Measures contained in NEP are mainly focussed on perfection of working skills and support to business activity. The employment promotion measures are closely linked with implementation of the *Joint Assessment of Employment Priorities in Latvia* signed by Latvia and the European Commission and the Development Plan for 2004–2006. The funding perspective of activities included in the *National Employment Plan* is linked with the European social fund (ESF), which is the main EU financial instrument for development of human resources and perfection of functioning of the labour market.

From January 1st, 2004 the minimum wage in Latvia was raised from 70 LVL till 80 LVL. The previous increase was in January 2003. In May 2003 the government approved the concept on the minimal wage, which foresees in the next seven years to raise the minimum wage till 50% of the average gross wage of the employed for the preceding year. At the moment the minimum wage equals to about 37% of the average gross monthly wage of the employed people.

Latvia has started several important reforms to address social issues. State funded second level pension scheme was launched on July 1st, 2001 and it is one of the most progressive in the countries of transition. This marked the end of introduction of a three-tier pension system. The pension reform in the area of legislation is completed. The pension age will be gradually increased. In comparison with the previous system where the pension age for women was 55 years and for men – 60 years, the new system will equalise the pension age (62 years) both for men and women by the middle of 2008.

In June 2002 the Cabinet of Ministers accepted the *Concept on Education for 2002–2005*. The concept is the foundation for the third phase of development of education aimed at increasing quality of education in all phases of learning, to ensure access to education in the context of life-long learning and to increase cost efficiency of education. Declaration on the Intended Activities of the Cabinet of Ministers foresees promoting growth of the role of education in the society and training of new specialists in line with the needs of the Latvian economy.

The aim of the long-term development strategy of Latvia is to ensure the transition from the labour-intensive economy to the knowledge economy and in this way to reach the average per capita GDP levels of the EU member states in the next 20–30 years.

*Long-term Economic Strategy of Latvia* defines basic positions of the economic policy. It is planned to change the currently dominating model of the Latvian economy as it is mostly based on the use of cheap labour and production with low value added. The offered way: intensive use of knowledge and high technologies, transition from labour-intensive economy to knowledge-intensive economy. This may be reached by simultaneous revival of traditional sectors of national economy on a modern technological base and the development of new, post-industrial knowledge-intensive sectors. Latvia will create the *new economy* and the importance of knowledge as a resource and wealth will grow in all sectors, also in traditional sectors, products or occupations.

The model of the economy foreseen in the long-term Economic Strategy is detailed out in the *Industrial Development Guidelines of Latvia*. This document specifies basic measures to be performed by the state in order to implement the set priorities and increase competitiveness of industry in the medium-term. Advanced intellectual products of Latvia owned by a resident or an enterprise registered in Latvia will become the main factor for reaching high growth rates of GDP. Development of sectors, which are based on high technologies, and use of skilled workforce is treated as a priority.

To ensure the development of knowledge-based sectors and growth of products with a high added value the government of Latvia emphasises the need to create the environment which is favourable to innovations and promote cooperation between industry and research and development sector.

On April 1st, 2003 the Cabinet of Ministers adopted the *National Innovation Programme for 2003–2006*. The aim of this programme is to promote the growth of state innovation capacity. Within the scope of the programme it is planned to carry out activities promoting innovation and coordinate them with other government documents and programmes and to start innovation promoting activities, which include the creation of the united National Innovation System, innovation-friendly environment, support mechanism to introduction of innovative solutions in commercial activity and creation of the world class innovation infrastructure. The Action Plan for implementation of the *National Innovation Programme* of 2004 has been developed. It contains recommendations of the World Bank in the area of perfection of the national innovation system.

## **2 The Latvian integration in the European Union**

On December 13th, 2002 in Copenhagen Latvia officially completed accession negotiations started by the conclusion of the Treaty of Europe and on April 16th, 2003 signed the Treaty of Accession. This was followed by the referendum on September 20th, 2003 where citizens of Latvia had to make their final choice with regard to the EU accession. Citizens of Latvia, the same as citizens of Estonia, Lithuania, Poland, Czech Republic, Slovakia, Slovenia, Hungary and Malta decisively voted in favour for joining the EU (at the referendum).

Finally, for Latvia and other nine accession countries to join the EU on May 1st, 2004 it was necessary that all 15 present Member States ratify the EU Treaty of Accession according to the national procedures of every country. Many of the EU Member States have already accomplished this task by the end of 2003.

Whilst Latvia is still preparing to become a fully fledged EU Member State already since April 16th, 2003 Latvia has been granted an observer status in the EU institutions – the European Council, European Parliament, Council of Ministers structures as well as in working groups and committees of the European Commission. This will allow Latvia to integrate into processes proceeding in the EU better, express Latvia's positions and protect national interests between April 2003 and the moment of accession. Consequently, the Prime Minister of Latvia and the Minister of Foreign Affairs had the opportunity to participate actively in the discussion of the draft of the new EU Constitution. Branch ministers in 2003 could express and defend the national interests of Latvia in the areas important for the Latvian economy also within the framework of the EU Council of Ministers. Experts of public administration have been involved in work of working groups and committees of the EU Council of Ministers and the European Commission focussed on the development and discussion of the drafts of EU legislation.

From May 1st, 2004 Latvia is EU Member State!

Source: <http://www.europa.eu.int/comm/enlargement/>

### 3 Improvement of business environment

The paramount task of a business development policy is to create the environment favourable for business, to stimulate initiative of entrepreneurs and to reduce general risks, to eliminate obstacles for business development, promote stability and efficiency of financial systems and capital market to stimulate competitiveness of Latvian enterprises in the market.

*The Action Plan for Improvement of the Business Environment* is implemented in Latvia since 1999. *The Action Plan* is an inter-ministerial policy-planning document encompassing directions of work to improve the business environment; activities to be accomplished, the responsible institutions, performance indicators and implementation deadlines. *The Action Plan* also includes the tasks to amend legislation, review and simplify procedures, improve coordination between various institutions, prepare and publish information and train workers of the public sector. *The Action Plan* has assisted in reaching a substantial progress in business environment – to decrease administrative barriers, to simplify tax administration, streamline administrative procedures of customs clearance and border crossing, to provide easier access to information and better protection of interests of investors. The Latvian Development Agency in cooperation with other public administration institutions has accomplished substantial reforms and improvements in the field of company registration, tax policy, customs legislation, procedures and border crossing rules, construction and real estate development, etc.

On July 31st, 2003 the Cabinet of Ministers passed the new *Action Plan for Improvement of Business Environment*. The plan includes 35 activities aimed at improvement of business environment and identifies ministries and institutions responsible for implementation of this plan. The Cabinet of Ministers has entrusted the Latvian Development Agency the task to supervise implementation the *Action Plan* and to institutionalise the dialogue between the government and business community.

There is another important initiative accomplished alongside with other attempts to liquidate administrative obstacles for investment in Latvia. *The Foreign Investors Council (FIC)*, which consists of leaders of foreign companies operating in Latvia once in a year organises a meeting with the highest-level government officials of Latvia

and heads of the biggest international enterprises representing a variety of sectors and countries. *The Action Plan for Improvement of the Business Environment* is included in the agenda of these meetings already since the second high-level meeting. The recommendations expressed there are later incorporated in the plan. The next high-level meeting between the government of Latvia and the Foreign Investors Council is scheduled for March 16–17, 2004.

Measures of business environment improvement have received assistance from the PHARE programme, the World Bank/FIAS, Swedish International Development Agency and other international financial organisations. The World Bank/FIAS have developed and modelled their self-assessment methods after pilot projects carried out in Latvia. The European Commission DG Enterprise in 2002 granted the ‘CC Best’ status to these projects, which means that activities accomplished in this area in Latvia can serve as an example for other EU candidate countries striving to improve their competitiveness. Also, the European Commission Progress Report 2002 on Latvia states, that “there are serious attempts made to improve the business climate”.

The Latvian Development Agency and the World Bank approximately once in two years carry out the research of the impact of administrative procedures on the business environment. The study serves as a basis for comprehensive attempts to improve the business environment, which have resulted in outcomes, which have been highly evaluated by the European Commission and the European Bank and set as a source of experience for other countries.

In autumn 2003 the Latvian Development Agency carried out a survey of activities aimed at improvement of business environment. The survey was carried out in collaboration with the World Bank and a sociological research firm *Latvijas Fakti*. The study, which is performed on a regular basis, allows comparing tendencies of business development, identifying areas in need of new reforms and allows measuring efficiency of different activities aimed at improvement of the business climate. The survey helps to develop support measures for small- and medium-sized businesses and to study the opinion of entrepreneurs in regard to the work of state and municipal institutions.

On December 20th, 2001 the Saeima adopted the *Law On Entry Into Effect of the Commercial Law*, which stipulates:

- the procedure of registration of enterprises in the Register of Enterprises
- interpretation of terminology in the transition period
- the transition period for companies registered in the Register of Enterprises and their branches, subsidiaries and representation offices
- series of special provisions
- transition regulations, with a reference to the respective laws and CM regulations, which lose effect on January 1st, 2005.

The law also requires drafting laws on unions and foundations, vocational work, insolvency, management of state and local government capital shares in capital enterprises and other necessary amendments to the existing legislation.

The government has recently reduced and is planning further reduction of the tax burden on businesses.

The law *On Annual Reports of Enterprises* prescribes a simplified reporting system for the companies that match the criteria of a small business.

Taxpayers financing projects aimed at reduction of pollution of the environment and consumption of natural resources by implementing technological improvements and nature conservation measures can benefit from discounts of the natural resources tax. If entrepreneurs implement a voluntary packaging materials management programme according to the principles of the Latvian Green Dot, the Ministry of Environment, on the basis of recommendations issued by the Packaging Management Council, may award the discount and exemption from the natural resources tax.

#### 4 Small- and medium-sized enterprises

Small- and medium-sized enterprises (SME) comprise the major part of Latvian economy and play a significant role in employment and GDP growth.

There were 42,549 economically active enterprises in Latvia in 2002, 42,275 or more than 99% of which fell in the category of SME (taking into account only number of employed). The distribution of economically active SME in Latvia according to the size is similar to the EU Member States and EU Accession states: micro enterprises – 76%, small enterprises – 20%, medium-sized enterprises – 4% (See Appendix 1).

Promotion of development of SME is considered a priority in Latvia. Therefore the Ministry of Economics has developed and on October 27th, 2003 submitted to the Cabinet of Ministers the draft of the long-term *Basic Guidelines of the SME Development Policy in Latvia*.

The goal of the guidelines is to promote a sustainable development of SME in the whole territory of Latvia and to create a favourable, encouraging and supportive environment for the development of business ideas, creation of new companies and growth and improvement of competitiveness of existing SME.

The *Law on Commercial Activities* lays down the definition of small- and medium-sized commercial enterprises being the commercial companies employing less than 250 employees, where net turnover does not exceed 23 million LVL or total balance sheet value is under 15 million LVL and where less than 25% of capital parts (shares) or voting rights belong to one commercial company or several commercial companies which do not comply with the above criteria.

Within the scope of the *Latvian SME programme (2003–2006)* all small- and medium-sized commercial companies are divided into three groups in line with the definition established in the EU legislation:

- medium-sized commercial companies – companies employing 50–249 employees, annual turnover – below 23 million LVL or the total balance sheet value under 15 million LVL
- small commercial companies – commercial companies employing 10–49 employees, where annual turnover is below 4 million LVL and the total balance sheet value is under 3 million LVL
- micro commercial companies – commercial companies employing not more than nine employees where annual turnover is below 0.5 million LVL and the total balance sheet value is below 0.4 million LVL.

The SME Development Policy is focussed on five key directions:

- perfection of entrepreneurial environment of SME
- promotion of availability of financing of small- and medium-sized business
- development of human resources and new business initiatives
- promotion of market competitiveness of SME
- promotion of SME development in territories with a relatively low index of socio-economic development.

The guidelines also foresee implementation of the policy, which is based on the best practice of companies of the developed countries and the activities outlined in the European Charter of Small Enterprises simultaneously respecting also the specifics of the development problems of SME in Latvia.

Taking into consideration the scarce budget resources and principles of free market and fair competition the Guidelines stipulate state intervention in the areas with significant market failures with regard to SME. The document is focused on creation of conditions promoting advantageous conditions for SME (including also tax policy) rather than giving direct financial or other support for individual companies.

To ensure implementation of the Guidelines the ministry will develop medium-term programmes. These programmes will detail out the tasks to be accomplished according to the Guidelines and will support this with relevant financial plans, names of responsible institutions, planned outcomes and performance indicators.

According to the decision of the Cabinet of Ministers with regard to the Guidelines, the Ministry of Economics submitted to the State Chancellery the draft of the programme on *Development of Small and Medium-Sized Enterprises of Latvia in 2004–2006* (See Appendix 2). An inter-institutional working group has been set up to deal with this task by the order of the Ministry of Economics of November 7th, 2003. This working group will comprise representatives of ministries and other public institutions together with the representatives of the Cooperation Council of Small and Medium-Sized Enterprises and Crafts, Confederation of Employers of Latvia, etc. and also NGOs working in the area support of interests of SME.

Activities to implement the guidelines and the programme will be developed in close connection with the plan of utilisation of EU Structural Funds as the majority of support activities of SME foreseen in the programme will be realised with attraction of cofunding from the EU Structural Funds. Because of this consideration also the further programming periods of SME development policy implementation are harmonised with the next National Development Plan to ensure that co-financing from the EU Structural Funds is also available and reserved in the next development plans.

## **5 State consultative support for starting businesses**

The Ministry of Economics has developed *The Consultative Support Programme for Starting Businesses* which is approved by the State Support Supervision Commission (Decision No. 55 of September 5th, 2003). The aim of the consulting programme is to facilitate formation of new companies and the development of the existing ones, to

strengthen their position in the domestic market and in further perspective also in the single EU market.

Consulting will be delivered in the areas of:

- taxation, accounting, loans and other financial issues
- preparation of a business plans
- market research
- registration of sole proprietorship or a limited liability company, permits, licences and other documents needed to start and operate a company
- specific sectors of work of a starting enterprise, specificity of the branch, investment and payback periods
- mandatory and voluntary EU quality requirements
- preparing applications to apply for support to the EU Regional Development Fund.

The total funding of the programme for 2003 amounts to 40,000 LVL. Total consulting costs in 2003 equal to 80,000 LVL, of which 40,000 is going to be paid from the state budget (50% of total costs) and 40,000 LVL will be paid as cofinancing by companies (50% of total costs).

The Ministry of Economics plans to develop similar support programme of consulting small- and medium-sized enterprises also for 2004.

## **6 SME development crediting programme**

Since 2000 the Mortgage and Land Bank of Latvia (hereinafter MLBL) implements the programme of support for crediting SME development. The insofar implementation of the programme has essentially promoted access of capital to SME and encouraged more active involvement of commercial banks in offering loans to SME.

On November 26th, 2002 the Cabinet of Ministers approved the Programme of Crediting Latvian SME (second phase) for the next three years foreseeing state guarantees in the amount of 20 million LVL to MLBL to enable the bank to borrow the necessary resources for crediting of SME in the financial market.

More than 2650 new jobs have been created during the period from January 1st, 2000 till September 30th, 2003. Average costs of creating one job (size of a loan) constituted €17,000. One loan on an average resulted in the creation of three new jobs.

From the outset of the programme till September 30th, 2002 MLBL has granted 957 loans, of which 60% of loans to SME were issued within the scope of the state guaranteed credit line.

Loans with special support facilities were granted to 325 specific SME for the amount of €13 million (approximately 50% loans issued within the scope of the state guaranteed credit line). The majority of loans with the support were issued to SME owned (to the extent of at least 51%) by women or managed by women or where women constitute at least 75% of employees (approximately €6 million). This is followed by loans to SME in supported regions (approximately €4 million) and to developing SME with insufficient pledge or collateral possibilities (approximately € 3 million).

SME's own participation in SME development crediting programme constituted approximately €25.6 million. This means that thanks to this SME development crediting project the Latvian economy received approximately €71.5 million (including from loans of MLBL issued to SME).

## **7 Assistance to small- and medium-sized enterprises in the European Union**

On June 19–20, 2000 the EU Member States during the meeting of the European Council approved the European Charter for Small Enterprises. This is one of the most important EU political documents to reach the goals set out in Lisbon. The Charter recognises the important role of small enterprises in the development of competition, innovation and employment considering these enterprises as the main driving force behind social and local integration in Europe and basis for economic growth. On April 23rd, 2002, by signing Maribor Declaration in Slovenia, Latvia together with other EU accession countries joined the European Charter for Small Enterprises and joined the commitment to work according to ten charter lines for actions. In October 2003 Ministry of Economics in cooperation with other state institutions submitted the second report on implementation of the Charter to the European Commission.

The European Council in December 2000 accepted a decision No. 2000/819/EC on the Multi-Annual Programme for Enterprise and Entrepreneurship, and in particular for small- and medium-sized enterprises (SME) 2001–2005. The programme is a tool to achieve the goals set in the European Charter for Small Enterprises. Latvia joined the Multi-Annual Programme in 2002.

The goals of the Multi-Annual Programme are achieved through a range of activities, which may be divided into such sectors as network of Euro Info Centres (EIC), financial instruments, development of policies.

The goal of EIC is to ensure SME better access to information about the EU, EU policies, legislation, quality requirements and programmes, thus assisting in business development and ability to get adapted in the new market. The EIC network with 39 centres was established by the 23rd directorate general (DG Enterprise) of the European Commission in 1987. In 2003 there were already 255 operating EIC, 14 Euro Info corresponding centres, 340 relay points and 31 associated members in 42 countries (including EU member states, EU candidate countries and countries of the European Economic Area). The first EIC in Latvia was established already in 1997 under the auspices of the Latvian development agency (LDA). In 2003 the competition organised by the EC and coordinated by the Ministry of Economics on opening of the second EIC was completed. EIC-2 has started its work under the auspices of the Latgale region Development Agency.

The European investment fund (EIF) carries out financial instruments of the EU Multi-Annual Programme and it is targeted towards improvement of financial environment for entrepreneurial activity and particularly for SME. EIF that is a cooperation partner for the EU member states, and candidate countries in the area of providing guarantees for project implementation linked with drawing risk capital. In March 2003 EIF in cooperation with the Ministry of Economics started to study also potential partner institutions in Latvia to realise further cooperation. The Mortgage and Land Bank of Latvia was selected as a cooperation partner. MLBL has made a conceptual

agreement with EIF according to which the EIF will guarantee to cover 50% of losses that may occur as a result of the SME crediting programme. EIF guarantee will refer to loans issued during 2004–2005 to SME employing up to 100 persons (maximum €1.1 million). The end of 2003 will conclude the agreement. Thus EIF support will be available from 2004.

The third part of the Multi-Annual Programme is focussed on the SME policy development through the business environment simplification task (BEST) and horizontal projects. The EC and national administration institutions actively cooperate in BEST projects to gain better understanding on various issues relating to entrepreneurial activity to identify cases of the best practice and evaluate choice of policies. Latvian experts from the governmental and non-governmental organisations participate in the work of working groups of the BEST and horizontal projects since 2002. In February 2003 the Ministry of Economics prepared the first report on the work of experts in the working groups and this report has been posted to the ministry's home page.

It is also important to mention the project 'support measures and initiatives for enterprises databases (SMIE DB)' under the EU Multi-Annual Programme. The main goal of the project is to assist state institutions and business support organisations to carry out comparative analysis and evaluate the European business support measures by identifying the best practice and sharing the best experience. More than 2500 support measures are included in the databases referring to 26 countries – the information is in English and also in the language of the country of origin of the measure. Data is updated every six months. In September 2003 also SME support measures implemented in Latvia were added to these databases (in English). Currently preparation of the Latvian version is in progress.

On the basis of the information obtained within the framework of the project of the Multi-Annual Programme, the Ministry of Economics has prepared and posted on its homepage the information on Latvia's SME support measures in the Latvian language. Now it is possible to visit the website and read the basic information about relevant laws fostering the development of SME, concrete SME support instruments and access to them.

## **8 The Government's main goal for long-term development**

The Government has set the main goal for long-term development, which is to reach the average per capita GDP level of the EU Member States in the next 20–30 years and to ensure its substantial growth in the medium-term.

The most important and urgent tasks of economic and social policy to reach the above goal are the following:

- To maintain stable macroeconomic environment, which should be done with the help of coordinated fiscal and monetary policy. Latvia is interested to join the European monetary union in line with the strategy developed by the Bank of Latvia.
- To develop and implement exports promotion policy in line with the new priorities in the area of foreign trade to actively promote international competitiveness of Latvian enterprises, promote their entry into new markets and reinforce the position in the existing ones.

- To perfect the institutional environment of business, by updating and simplifying legislation, eliminating obstacles to business activity, creating a tax system favourable to business, promoting stability and efficiency of the financial system and capital market, etc.
- To ensure equal and fair competition. One of the basic tasks of the competition policy is to encourage the opening of monopoly sectors for competition, which results in increased efficiency in monopoly sectors of economy and the consequent reduction of the share of monopoly prices in production costs.
- Continue fighting corruption and reduce possibilities of operating in the grey economy sector.
- To streamline the system of state assistance funds, to provide clear information to businesses on where and in what conditions they may receive assistance from the state to raise competitiveness of their business. The state should develop procedures for funding of state-assisted projects from the state budget and EU structural funds focused on the development of new products and technologies, upgrading of commercial infrastructure, consulting and participation of commercial companies in international fairs and trade mission, training, retraining and continual training of employees, risk capital of small- and medium-sized commercial companies, counselling services at the outset of commercial or self-employment activities.
- To wider use public and private partnership mechanism, particularly in the area of work with the EU structural funds for the development of infrastructure, forming partnerships with private capital.
- To ensure higher levels of consumer protection by continuing perfection of legislation and mechanisms of enforcement of the law.
- To encourage innovations, cluster formation, research and development in enterprises (R&D), introduction of high technologies by creating the environment favourable to innovation; state support to innovative enterprises and infrastructure (research and knowledge centres, technological centres, business incubators, development of high technology enterprises).
- To implement the policy aimed at lessening social and economic disproportion. The primary task in this area is to decrease unemployment being the main reason for poverty and social exclusion. Special attention should be devoted to less developed areas. The state should create real tools and legal instruments to encourage businesses to invest in the disadvantaged areas.

## **9 Basic concepts for the development policy of the SME in Latvia**

For the purpose of this document the term ‘enterprise’ is understood as a business, a foreign subsidiary business organisation entered in the Business register, an enterprise (a business company) entered in the Enterprise Register, its subsidiary, branch, independent representation, cooperative corporation, or a physical person engaged in economic activity (e.g., a craftsman, individual worker, etc.). In its turn, the term ‘entrepreneurship’ is understood also as business activities.

In order to improve the support policy of entrepreneurship and, particularly, have the SME, in compliance with the best experience of the EU, Latvia participates in the SME support activities. On April 23rd, 2002 Latvia joined the European Charter of Small Enterprises and binding itself to build its national development policy of the SME according to the following directions of its activity:

- educational and training programmes aimed at raising the entrepreneurial activities
- cheaper and faster establishment of an enterprise
- legal, regulatory and administrative environment favouring the SME development
- availability of skills and proficiency
- access to the internet
- access to the Common market in such spheres as e-commerce, telecommunications, services, government purchase and inter-state payment systems, as well as access to new markets, and a possibility to compete on equal terms, which are essential for the development of the small enterprises
- a tax policy that is favourable for the SME and the new entrepreneurs, as well as an availability of the financial support services
- strengthening of the SME technological capacity
- adaptation of the most successful e-commerce models and support to the SME–information and entrepreneurship support systems, networks and support services
- efficient representation of the SME interests in the EU and on the national level.

At present the main instruments of the SME support policy are:

- *The credit programme for the SME development*, which was introduced in order to facilitate an access for the SME to the financial resources, as well as to lower their costs. The Latvian Mortgage is implementing the programme and Land Bank (LMLB) in agreement with the crediting conception accepted by the government in November 1999. Within the framework of this programme 901 loans were granted during the period from January 17th, 2000 to June 30th, 2003, the net loans being €43.1 million, which has promoted the creation of 2,472 new jobs. Thus, on the average, every 17,400 LVL have sponsored 1 vacancy.
- *The regional fund (RF)*, created in 1998 with an aim to decrease the costs of credit resources of the SME in areas with a particularly low index of socioeconomic development. In the period from 1998 to the end of 2002 the RF contribution to the entrepreneurship development projects in specially supported regions has been 4.3 million LVL, which has promoted opening of more than 3,000 new permanent and 3,500 seasonal vacancies, and allowed to retain the existing 3,900 jobs. One invested lat of the RF has attracted more than 26 lats from the entrepreneurs and municipal enterprises and almost 2 lats from other sources.
- *The guarantee mechanism of the SME*, implemented by the Latvian guarantee agency (LGA), has been set up to ensure guarantees for the beginning entrepreneurs, as well as to enhance and evolve entrepreneurial activity. At the beginning of 2003 new guarantee regulations were worked out in cooperation with the Latvian

Association of Commercial Banks. In parallel with them, the LGA has been transformed from a non-profit organisation into a profit-bearing enterprise in the form of a SIA (limited liability company). The LGA started its full-fledged activity on June 1st, 2003. The maximum guarantee amount is 25,000 thousand LVL, from which the LGA can take up guarantees for entrepreneurial credits up to 70% of this amount. The LGA does not guarantee credits connected with agriculture and trade.

- *The state support to the SME in terms of consultations and professional training.* In 2003 the Ministry of Economics has started a support programme providing consultations to the SME and beginning entrepreneurs, assigning 40,000 LVL from the state budget for this purpose.
- *Support programmes aimed directly at the support of the small- and medium-sized enterprises.* Till October 17th, 2003 the State Support Supervision Commission has endorsed the following support programmes: Crediting of the development of the small- and medium-sized entrepreneurship (2001–2010), the order of rendering state support to Latvian enterprises for the participation in international exhibitions and fairs (commercial missions) (2001–2007), the order of rendering state support to Latvian enterprises for a single research of the external market (2001–2007), the programme for the development of non-agricultural entrepreneurship (2002–2004), the Latvian Export marketing support programme (April–December, 2003), the loan guarantee support programme of the Latvian Guarantee Agency (2003–2006), the project preparation support programme for the European Regional Development Fund (June–December, 2003), the crediting programme of the small- and medium-sized enterprises (the second stage) (2003–2013), the consulting support programme for the entrepreneurial beginners (till 31st December 2003), and the development of the entrepreneurship (business activity) in particularly supported areas (01st January 2004–31st December 2006).

General formulation of the problems, the solution of which requires implementation of the SMS development policy

- *Entrepreneurial environment.* The competitive ability of the SME sector cannot develop without a favourable entrepreneurial environment. The competitive ability of national economy depends on how competitive the state tax policy is, what the capital market, the infrastructure, educational system and the efficiency of state support are like, how coordinated and stable the entrepreneurial legislation is. A conclusion follows from the entrepreneurs' inquiry results and the conclusive reports made at the meetings and conferences of nongovernmental organisations representing the SME interests that many of these factors are not favourable in Latvia for the evolution of entrepreneurship; besides, the smaller an enterprise is, the greater is the effect of the problems just in this field. In spite of the fact that Latvia has attracted successfully direct foreign investments, the entrepreneurial environment in Latvia cannot be still regarded as maximum favourable, particularly, within the context of the development of the small- and medium-sized entrepreneurship. The establishment index of new enterprises is very low, and the number of enterprises per 1,000 of the population in 2002 was only 18.3, which is considerably lower than the respective index (51) in the EU member states.

- *Availability of financing.* Although recently the chance of obtaining external funds has considerably increased, the availability of the working and capital financing is a significant obstacle to the entrepreneurial activity and competitive ability both at the small- and medium-sized enterprises and among the beginning entrepreneurs. The absence of stringent requirements for the support combined with the lack of credit history and experience (profit, index of growth, etc.) affects the entrepreneurial activity adversely. The guarantee and investment funds are not sufficiently developed at present, and they are not on the capitalisation level required for the SME development. The problems in the sphere of the availability of external funds are more evident outside Riga; the problem of the availability of external funds has an explicit territorial dimension. At the beginning of 2003, when the national interest rate was 11% (considerably higher than the average rate in the EU of 6%), the interest rate in the regions distanced from Riga is 15% because of a greater risk.
- *The personnel resources.* The potential enterprises often face insufficient skill of entrepreneurial management, entrepreneurial activity and technical incompetence in order to work out high-quality and high-grade business plans, poor knowledge of the management of finances, cash flow and organisational culture working in global economics. To increase the competitive ability of the Latvian small- and medium-sized enterprises, it is necessary to implement a purposeful policy of human resources (entrepreneurs and workers). Latvia has to ensure the necessary conditions for a shift to knowledge-intensive production, with simultaneous training of a sufficient number of qualified specialists for the SME.
- *The SME competitive ability.* According to the investigations carried out by international organisations, Latvia, by its competitive ability, occupies the last place among the Baltic States. Further, although the extent of Latvian export has grown remarkably in the recent years, the situation will change rapidly after its entrance into the EU because of the higher competition; many of the still existing advantages of competition will disappear. An urgent problem is also that the enterprises of Latvia working by the EU quality directives need information on the product standards and the new methods of production. There are no instruments available in Latvia for the evaluation of the product quality.
- *The SME development in areas with a relatively low index of socioeconomic development.* During the recent decade negative trends have been observed in the socioeconomic development of Latvia – rapid growth of the country's economic centres with concurrent stagnation, or even regress, in the territorial development of the outlying area. This has caused increased contrasts between towns and rural areas, as well as between the central part of the country and the periphery. Integrated development of rural territories, including non-agricultural entrepreneurial activity, is a prerequisite for well-balanced development of the state.
- *Administrative capacity of the state and non-governmental organisations* in the field of the development and implementation of the SME policy, as well as the acquisition of the EU structural funds is presently insufficient. The chief reasons for this are the limited financing ability from the state budget, the lack and turnover of human resources, the insufficient competence and qualifications of the policy makers and implementers, as well as no professional training of the existing and potential

specialists. In order to promote successful implementation of the entrepreneurial policy, it is envisaged within the framework of the EU technical support programmes to make significant investments (of approximately €20 million) in order to increase administrative capacity by attracting a maximum large amount of the EU structural funds. These measures are aimed both at the improvement of the technical equipment and attraction of additional human resources. In order to raise administrative capacity, it is intended in 2004 to assign, as co-financing, about 900,000 LVL from the state budget, including the Latvian Development Agency and Ministry of Economics.

#### Basic principles of policy

- to keep strictly to the principles of the free market economy and regulate them only when there are certain market gaps in the respective field, the chief emphasis being laid on the creation of favourable conditions for the SME economical activity (including the tax policy), rather than on direct support to individual enterprises
- to build such a SME development policy, which would agree with the basic principles of the European Charter, with simultaneous adaptation to the SME specific, needs and conditions
- to adhere persistently to the policy of the EU member states and international organisations in the field of the SME and take over *the good practice*
- to implement such measures aimed at the evolution of the small- and medium-sized entrepreneurship that ensure optimum use of the state budget means in order to gain maximum effect with a minimum share of the state budget
- to recognise and popularise the results of Latvian entrepreneurs by way of examples of good practice.

#### *9.1 The goals of the policy*

The goal of the SME development policy is to raise entrepreneurial activity, particularly, in areas with a relatively low index of socioeconomic development, to strengthen the SME competitive ability, and to enhance the growth in the added value created by SME.

It is intended to achieve this by implementing the following political goals and sub-goals:

- to create a favourable entrepreneurial environment, particularly with respect to the SME
- to ensure availability of the financial support services both to the SME and the beginning entrepreneurs
- to develop human resources and promote the appearance and expansion of new entrepreneurial initiatives
- to facilitate the SME competitive ability in Latvian, EU and external markets
- to favour new entrepreneurial initiatives and the SME expansion in areas with a relatively low index of socioeconomic development.

### 9.2 *The results of the policy and the indices of their attainment*

The results of the macro influence and the (resultant) indices of their attainment:

- the growth in the goods and services export by 5–7% a year
- decrease in the unemployment level down to the average approximate 7% of the economically active population in ten years' time
- increase in real average salaries of the workers engaged in the private sector by 6–8% a year, retaining moderate inflation rate.

The results of the policy and the (resultant) indices of their attainment:

- the number of the economically active SME has grown from 18.3 to 32 enterprises per 1,000 of the population
- the number of the SME founded during one year has increased, on the average, by 10–15%
- the ratio of the cases when the SME have stopped their activity during the first two years of their life has decreased by 50%
- the number of the economically active SME engaged in priority (perspective) branches and regions supported by the state has grown, on the average, by 20–25% a year
- the total added value created by the SME has grown, on the average, by 10–13% a year
- not less than additional 50,000 people are permanently engaged in the SME sector.

### 9.3 *Directions of action to achieve the goals and results of the policy*

Direction of action: improvement of the small- and medium-sized entrepreneurial environment:

- permanent analysis of the condition and development of the SME sector; analysis of entrepreneurial environment (regulating entrepreneurship and the legislative, support policies, etc. connected with entrepreneurial activity), and the analysis and revision of its impact; proposals for the advancement of the SME activity (including the investment of the finances for further development), as well as introduction appropriate measures and activities
- constant and efficient dialogue between the state institutions and the SME
- ensuring a possible favourable fiscal climate for the SME (including favourable tax policy to advance the SME development in the aspect of the priority branches)
- removal of administrative obstacles to entrepreneurial activity and establishment of new enterprises

- expansion of the scope of publicly available information (about the results of the market and other sorts of research; information pertaining to state purchases; coordination of various state entrepreneurial support funds and the possibility to update the information about them), including the distribution of brochures and reference books
- promotion of exchange with efficient information between the state and the SME, including the use of the solutions of modern technologies, introduction of the e-management conception.

Direction of action: promotion of financial availability for the development of the small- and medium-sized entrepreneurial activity:

- improved availability of loans on preferential terms
- improvement of the mechanism of efficient assignment of loan guarantees
- formation of an efficient instrument for the insurance of import–export transactions
- improved availability of the risk capital financing
- elaboration and implementation of specific SME support programmes (the possible spheres of the specific programmes: co-financing for the elaboration of new SME products and development of the existing ones, introduction of quality systems; support to the laboratories set up for the needs of priority branches and accredited for the export market, the services of which are mainly used by the SME; support to meet the obligatory requirements – for instance, labour safety, environmental assessment, etc.)
- creation of financial support instruments (support programmes, grants, etc.) for specific target groups – juveniles, women, long-term unemployed people, the disabled people, as well as a part of the society willing to be engaged in entrepreneurship in areas (regions) with a low socioeconomic development index
- facilitated financial consulting of the SME.

Direction of action: development of human resources and the initiative of new entrepreneurial activities:

- the active employment measures for the unemployed aimed at the development of their own businesses in the future
- providing information and consultations in connection with the acquisition of the EU structural and other funds
- promotion of several SME common projects to attract (co) financing, e.g., from the EU structural funds, rendering support to the connected SMR projects
- providing professional training and consultations to the SME managers, beginning entrepreneurs, as well as training of educated and qualified workers
- popularisation of entrepreneurship and related activities by means of mass media and civic organisations
- provision of information to the SME and beginning entrepreneurs according to *the one-stop agency principle*

- development of a business incubator network all over the country
- sponsoring business-related conferences, forums, seminars, special club activities, and the like
- promotion of the business idea – contests of ideas-projects, business games, as well as the creation of new and potential entrepreneurial organisations
- improvement of the access to high-quality entrepreneurship and business management education, including the spheres of adult further education and post-diploma training of enterprise managers
- promotion of the acquisition of interdisciplinary knowledge at higher educational institutions
- partnership stimulation in entrepreneurship
- propagation of practical and professional experience among the students – motivation of employers to create a possibility to undergo practice at their enterprise
- creation of a stimulation system (both on a state and municipal level) to propagate the entrepreneurial ideas, initiatives and activity, including the programmes for specific target groups.

Direction of action: promotion of the SME competition ability in the market:

- marketing advancement measures, export promotion
- quality raising measures (introduction of voluntary and compulsory quality requirements at enterprises)
- the infrastructure and (co) financing attraction support for the implementation and confirmation of the SME quality requirements (including for certificate obtaining, various tests, conformity assessment, etc.)
- measures (financial, infrastructural, informative and other kinds of support) concerning trademarks
- measures (financial, infrastructural, informative and other kinds of support) concerning patents, including access to the Community's patents.

Direction of action: promotion of the SME development in areas with a relatively low index of socioeconomic development:

- involvement of regional structures and municipalities in the strategic planning of the SME development policy, as well as in the elaboration of its subordinated programmes on a regional and territorial level
- organisation of educational seminars on entrepreneurial activity, its management, and the offered benefits and advantages in areas with a low index of socioeconomic development
- promotion of the acquisition of entrepreneurial ideas, knowledge and activity in regions and individual municipalities by providing informative and consultative support
- enhancement of non-agricultural entrepreneurship in rural territories

- elaboration and implementation of specific SME support programmes (the possible spheres of support: initial investments in the creation of new vacancies, environmental protection, energy saving, as well as the investments in real estate and environment infrastructure projects to be implemented outside Riga)
- state investments in the SME infrastructure development in perspective territories
- providing availability of credit interest subsidies to the SME.

In addition to these tasks within the scope of the programme, regional development indicators from various territories of the country will be taken into account in working out and introducing general support instruments for the promotion of the SME development, thus ensuring greater support intensity to the SME which operate in areas with a lower index of socioeconomic development.

#### *9.4 Evaluation of the impact on the state and the municipal budgets*

##### *9.4.1 Revenues*

- With reduced unemployment the state budget will be relieved due to the diminution of the unemployment benefits and the municipal budgets due to the minimisation of the support in order to ensure guaranteed minimum level of incomes.
- With the growing economic activity of the SME the total amount of revenues from taxes will increase in the state budget.
- According to the 'partnership principle of the state and the private sector', or refusal of the state from performing uncharacteristic functions (e.g., to ensure the GDP for the state and municipal institutions) and transferring them to the SME, the efficiency and expediency of the use of the state budget will grow.

##### *9.4.2 Expenditures*

- Extra expenditures in the state and municipal budget of 2004 are not expected. The measures envisaged by the programmes will be carried out within the range of the existing budgets and by attracting the EU structural funds and national cofinancing for the acquisition of structural funds.
- In the next period the expenses in the state budget will be planned in conformity with the measures laid out in the programmes, and in the context of the application of cofinanced EU structural funds.

#### *9.5 Planning further actions*

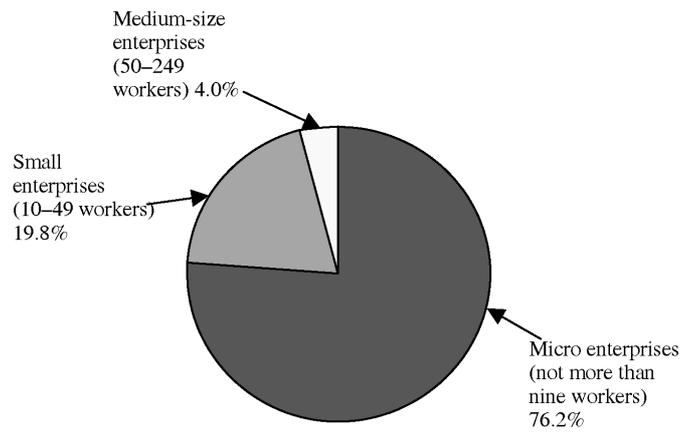
- To work out 'the development programme of the Latvian small- and medium-sized enterprises for the years 2007–2009'
- To work out 'the development programme of the Latvian small- and medium-sized enterprises for the years 2010–2013'.
- The Ministry of Economics is in charge of regular updating of the Basic Concepts, as well as the elaboration of the programme and scheduled measures mentioned in this section in fixed terms.

### Reference

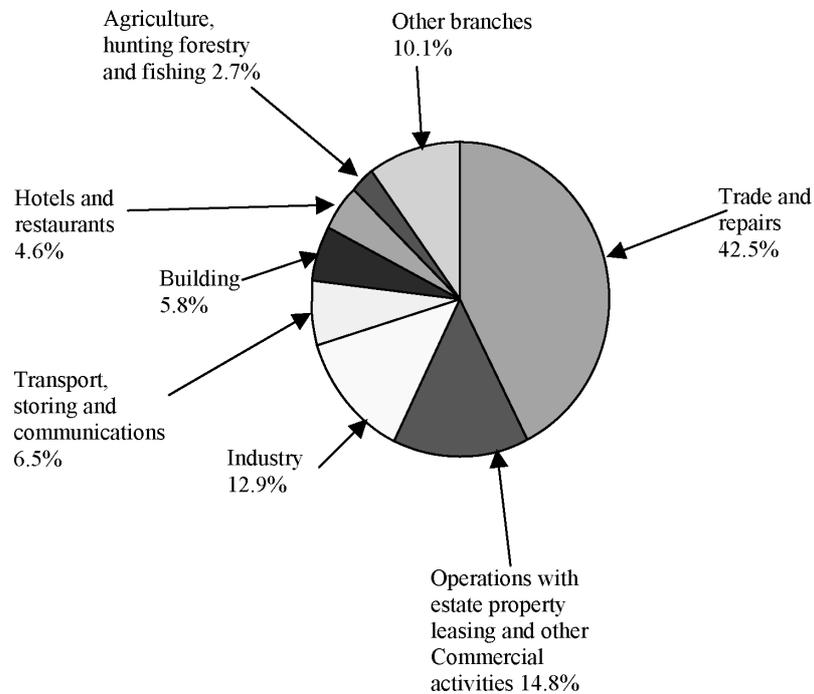
Economic development of Latvia (2003) *Report of Ministry of Economics*, Republic of Latvia, Riga, December.

### Appendix 1

**Figure 1** The SME distribution by their sizes



**Figure 2** The SME distribution by branches (number)



## **Appendix 2: The development programme of the Latvian small- and medium-sized enterprises for the years 2004–2006**

### **1 Introduction**

The development programme of the Latvian small- and medium-sized enterprises for the years 2004–2006 (the programme) has been worked out in order to ensure the attainment of the targets laid out in the basic concepts for the development of the small- and medium-sized enterprises (SME) confirmed by the Order No. 61 of the Cabinet of Ministers of January 29th, 2004. This is a medium-term policy-planning document set up for three years, and it comprises the measures of horizontal SME development.

The programme has been drawn up on the basis of paragraphs 3.1.1. and 3.1.2. of the government declaration, which prescribes,

“to determine the priorities and order how the state supports entrepreneurial activity, implements the support programmes for the small- and medium-sized enterprises, as well as promotes the development of the supported branches and territories.”

The aim of the programme is to enhance the attainment of the goals of the development policy of the small- and medium-sized enterprises formulated in the Basic Concepts by creating a favourable environment for entrepreneurship, removing administrative obstacles, stimulating the entrepreneurs' initiative, reducing general risk, enhancing the availability of finances, improving the system of support services for the entrepreneurial activity and its efficiency with simultaneous raising the competitive ability of Latvian enterprises.

The directions of action and tasks set out in the programme and the basic concepts are aimed at the attainment of the strategic state goal – raising the competitive ability and employment – and they agree with the priorities defined in the National Development Plan – the evolution of economy and enhancing the competitive ability, as well as the expansion of human resources and promotion of employment.

The SME development policy is in agreement with the main priorities of the state economic policy. The development of the SME sector in the country will intensify the production activities, avoiding economic and social disproportion and ensure balanced growth.

The SME form a great part of Latvia's national economy, and they play an important role both in the creation of the gross national product and employment. In 2002 Latvia had 42,549 economically active enterprises of which 42,275, or more than 99% were the SME. 42.5% of the SME were engaged in the service sphere (trade), however only 15% in production. On the whole, 69.9% of the workers in the private sector of the country were employed at the SME, which makes 63.2% of the GDP.

The main index of the SME development is the number of the SME per 1,000 of the population. In Latvia this index is 18.14, which is considerably lower than the average index (51) in the EU member states.

## **2 The link of the programme with the priorities of the government and ministry, and the support policy documents**

The following main policy documents form the basis of the development measures of the small- and medium-sized enterprises:

- basic concepts of the development policy of the Latvian small- and medium-sized enterprises
- Latvia's long-term economic strategy
- declaration on the intended activity of the Cabinet of Ministers
- the development plan of Latvia.

## **3 The goals and sub-goals of the programme**

The goal of the programme is to ensure the SME development support policy in agreement with the best practice of the EU states:

- to increase the entrepreneurial activity, especially in the areas with a relatively low index of socioeconomic development
- to strengthen the SME competitive ability and development, as well as
- to promote an increase in the added value created by the SME.

It is intended to attain this by implementing the following goals and sub-goals of the directions of action for the SME development policy:

- To create a favourable entrepreneurial environment, especially concerning the SME. A favourable entrepreneurial environment is one of the prerequisites for the SME development. The small enterprises are essentially affected by the amendments of the regulatory normative acts, the state tax policy, the development of infrastructure, as well as in other spheres.
- To ensure the availability of financial support services both to the SME and the beginning entrepreneurs. The availability of the working and capital financing is essential for the activity and competitive ability of the small- and medium-sized enterprises, as well as of the beginners. The SME sector faces significant obstacles and shortage of information in this sphere.
- To develop human resources and promote the appearance and development of new entrepreneurial initiatives. The most common problem in this field is the insufficient skill of entrepreneurial management, poor knowledge of business planning, the flow of finances, as well as other knowledge, which is essential for the development of an enterprise. It is necessary to introduce a purposeful development policy of human resources in order to ensure the competitive ability of the Latvian SME sector.

- To enhance the growth of the competitive ability of the SME in Latvian, EU and external markets.  
Latvia becoming a EU member state, competition will increase in several sectors; therefore it is necessary to work out a complex of measures ensuring the awareness of the small- and medium-sized enterprises about the conditions and the requirements, which they will face in the common market.
- To promote the appearance of new entrepreneurial initiatives and the growth of the SME in areas with a relatively low index of socioeconomic development.  
In Latvia the entrepreneurial activity is concentrated in economical centres, while the rate of entrepreneurship in the rest of the country is considerably slower, which has created contrasts between the towns and the rural territories. It is necessary to provide conditions for uniform development of entrepreneurship both in towns and in rural areas in order to ensure a balanced development of the whole country by taking special support measures there.

One of the primary tasks is the improvement of the institutional system, which would allow defining clearly the institutions responsible for the implementation of this and the following programmes. This is a prerequisite for the successful attraction of resources to implement the conditions provided by the programme both from the state budget and the EU Structural and other funds, international finance institutions, and the private sector. The improvement of the institutional system is necessary to achieve the results and resultant indices envisaged by the programme.

Measures are taken to put the programme into effect; the operative results, the resultant indices, as well as the financing – already existing in 2004 and the additional necessary financing for the coming years – and the responsible institutions are given in Appendices 1 and 2 of the programme.

#### **4 The results of the programme policy and the results of its activity**

Following the principles of market economy and after creating favourable conditions for the entrepreneurial activity the rate of export will be increased, and the level of unemployment reduced.

- the number of the SME established a year has grown by 5–7%
- the ratio of the cases when the SME activities were stopped during the first two years of their life has fallen by 50% in a decade
- the number of the economically active SME engaged in the priority branches and the state supported regions have increased by 20–25% a year.

#### **5 Financing of the programme**

Implementation of the tasks laid out in the programme has been set for a period from 2004 till 2006. The financing, to carry out the respective tasks, has been indicated as a volume of finance required for three years. The envisaged financing, if not specified otherwise, is shown in an indicative way, allowing the experts to evaluate the

approximate costs of the items concerning the implementation of the corresponding tasks; they may vary from year to year considering the specificity of the particular task and the selected project.

## **6 Management, coordination and evaluation of the programme**

On the whole, the management, coordination and evaluation of the programme is carried out by the Supervision Council set up by the Minister of Economics on the basis of the accounts of the activities submitted by the executive and cooperating institutions, this Council being formed of the representatives from state institutions and nongovernmental organisations (including the cooperation councils of the small- and medium-sized enterprises, Employers' Confederation, etc.). The executive institution is responsible for the introduction of each measure and the evaluation of its efficiency.

The Supervision Council of the programme can suggest the revision of the programme and make its amendments whenever necessary.